

Erdenes Mongol and State-Owned Enterprise Laws

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MONGOLIAN CONTEXT

As a holding company, the successful management of its operations, subsidiaries and joint ventures should be a key function of state-owned Erdenes Mongol. Clearly defining the rationale for the state-owned enterprise (SOE) and its mandate are important steps that would help guide Erdenes Mongol's decision-making. Doing so is likely to generate more revenue for the state, grow the Mongolian economy and improve public welfare.

Yet Erdenes Mongol's mandate, financial management and governance framework have never been clearly defined in law. The lack of an SOE or Erdenes Mongol law has led to *ad hoc* decision-making regarding the establishment of subsidiaries, associates and joint ventures as well as asset purchases. Without the guidance of a clear mandate and robust legislative framework, Erdenes Mongol has evolved into a complex company with interests not only in mining, but also mineral processing, unconventional oil and gas, roads, border crossing facilities, hotels, restaurants, power generation, engine repair, steel, trade promotion and asset management. It is unclear whether Erdenes Mongol is well equipped to engage effectively in all these sectors and projects that may require different skills, management and resources.

About this briefing

This briefing draws on the report *Wild Growth: An Assessment of Erdenes Mongol*, available at resourcegovernance.org/erdenes-mongol.



Erdenes Mongol could also benefit from financial and governance rules that encourage profit-making and protect taxpayer interests. Currently, many of the company's subsidiaries and joint ventures remain unprofitable or generate significant losses for the state. As a result, the company owes more than USD 350 million to creditors from just the subsidiaries for which we have information. Erdenes Mongol plans to seek billions of additional dollars in project financing for its metallurgical industrial complex project and energy export project.

Erdenes Mongol and its subsidiaries can become government budget liabilities if they take on debts or other financial obligations, or if they are used to transfer commercial risk from private sector partners to the public sector, without adequate collateral. Should the company not meet its debt obligations, taxpayers would need to bail out the company, as has happened in other parts of the world. What's more, each tugrik misspent is a lost opportunity for the state to invest that money into education, healthcare or productive infrastructure.

These issues, and others, can be addressed in large part with a new legislative framework. While a new law will not address all the challenges identified, it would help bring statutory clarity to Erdenes Mongol management, and improve intra-governmental coordination and consistent policymaking.

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STATE-OWNED ENTERPRISE LAWS AROUND THE WORLD

Several legislative options are available to the Government of Mongolia. In some countries, such as Argentina, Denmark, Hungary and Sweden, the companies law applies to state-owned enterprises.¹ This is the case in Mongolia today. However, in each of the cited countries, SOEs are operating entities (rather than regulatory agencies), subject to independent external audit, abide by international financial accounting standards and operate at global efficiency levels. Erdenes Mongol is not currently subject to audit by independent non-governmental auditors, does not comply with international financial accounting standards and its subsidiaries do not seem to operate at global efficiency levels.

In other countries, such as Canada, Costa Rica and Greece, each SOE is governed by its own law. These laws generally outline the company's mandate, governance structure, financial provisions and liability to the state, and public disclosure and audit requirements. They are often designed to provide detailed instructions to the board and company managers where there are gaps in the companies law or state-owned enterprise law or where additional guidance would be useful for sound decision-making.

1 OECD (2015) Board Practices and Financing for Latin American State-Owned Enterprises. www.oecd.org/daf/ca/Board-Practices-Financing-Latin-American-SOEs.pdf; OECD (2005) Corporate Governance of State-Owned Enterprises.

Table. Commons sections of state-owned enterprise laws

	SOE mandate or definition	List of SOEs	Strategic plan	Non-commercial activities	Shareholding	State financing	State liability	Sale of assets and equity	Role of parliament	Role of executive	Role of management	Board of directors	Code of conduct	Accounting	Reporting	Auditing
Afghanistan	X				X	X	X	X		X	X	X		X	X	X
China					X	X		X		X		X	X		X	X
Finland	X						X		X	X	X	X		X		X
Korea	X				X	X				X		X		X	X	X
Mexico		X			X			X		X	X	X	X	X	X	X
Namibia		X	X			X		X		X		X			X	X
New Zealand	X	X		X	X					X		X			X	X
Quebec (Canada)		X	X							X		X				
Vietnam	X		X		X	X	X	X		X	X	X	X			X

SOEs are covered by a general law in another set of countries, including China, Finland, Korea, Mexico, Namibia, New Zealand and Vietnam. Each of these governments have adopted laws that suit their own governance challenges and legal frameworks; for example, the New Zealand SOE law is comprehensive but does not apply to so-called "Crown Entities" which operate under the Companies Act nor does it include a code of conduct which is covered in other legislation. The table above provides a summary of the subjects covered in SOE laws around the world.

Most countries have a patchwork of legislation, which may include companies laws, SOE laws and laws for specific SOEs or categories of SOEs. For example, in Finland the companies law applies despite the existence of a separate SOE law. This explains why there are no reporting requirements in the SOE law.

Given our survey of legislation around the world, we would recommend that an Erdenes Mongol-specific law or an SOE law include the following elements: mandate and definition; strategic plans; non-commercial activities; shareholding; dividend policy; state liability; sale of assets and equity; role of parliament; role and tenure of management; board of directors; code of conduct; accounting; reporting; and auditing. To be effective, any such law would need to be rigorously enforced by the cabinet and responsible ministries and implementation effectively overseen by the State Great Hural, the Office of the Auditor General and the public.

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