



**LEGAL FRAMEWORK STUDY
ON ROYALTY TREATMENTS OF THE MINOR ELEMENT**

**Ulaanbaatar city
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Preface

The Australia-Mongolia Extractives Program (hereinafter as ‘**Program**’) is funded by the Australian Department of Foreign Affairs and Trade and is based on cooperation between the Australian Government and the Mongolian Government. Its second phase is under implementation between 2019 to 2023.

The objective of the second phase of the Program is to improve the investment environment of the mineral sector, which is important to the future development of Mongolia and to enhance cooperation between stakeholders so that stability and transparency of the mineral sector will be improved.

Under the activity plan covering 2020-2021, based on the request received from Ministry of Mining and Heavy Industry (MMHI), the Program is conducting study on treatment of the royalties (or in Mongolian ‘mineral reserve use payment’) with regards to the minor elements by involving mining, taxation, economics and legal expert team consisted from international and local experts so that MMHI would be capable of reaching common understanding among Ministry of Finance and General Tax Office and figure out differing positions and grounds expressed.

In this regard, the local legal expert conducted such study within a currently effective legal sources of Mongolian on royalties, noted its findings and made respective recommendations. Due course of this task implementation the local legal expert was involved in e-workshops organized among representatives of the relevant state organizations and pursuant with the issues raised the focus of this study rested on royalty framework of the hard minerals or metals at defined processing stages of ore, concentrate and product.

Pursuant with the Mongolian legal framework, the core principle on mineral wealth ownership and utilization is same as common international trends, meaning that mineral wealth contained in the subsoil is owned by the state as public property and utilization of such wealth shall be done in accordance with the laws. However, it shall be noted that with regards tax policies, as matter of sovereignty it is defined independently by the Parliament of Mongolia and calculation, imposition principles, perspectives and methods may differ from other countries.

It is understandable that each country defines its royalty regimes on its own, considering number of factors such as its socio-economic, foreign trade, heavy industry development aspects, state and mineral sector development policies, types of mineral wealth it has, technological enhancement level of its mineral sector, mainly exploitation and processing capacities, international commodity market situation, competition strategies, thus no universal scheme could be defined.

With regards Mongolia, we assume that the Parliament of Mongolia (or in Mongolian ‘State Great Khural of Mongolia’), Government of Mongolia and respective state organizations such as ministries and agencies are defining relevant legal frameworks, rules, and regulations for royalty treatment within their legal authorizations considering those factors accordingly.

Under this study, state policies studied covering period of from 2006 up to date as to match legal framework defined by the current Mineral Law’s approval in 2006. The state policies include Long Vision-2050, State Policy on Mineral Sector, Government Action Plan 2020-2024, State Development Direction between 2021-2025.

In terms of legal documents, such as laws, rules, and regulations, Constitution of Mongolia, Law on Subsoil, Minerals Law, General Tax Law, Law on Value Added Taxation, Law on Investment are studied along with secondary rules and regulations approved accordingly as relevant with the royalty calculation, imposition, payment, and reporting regimes.

It shall be noted that this royalty matter related with the minor elements contained as substitute element besides core mineral ore, concentrate or product, is not the simple issue of how to impose, but shall be studied thoroughly considering its direct and indirect impact on mining sector development, tax burden on local mining companies, impact on economic feasibility of the projects, their competitiveness at international commodity markets etc. The reason is due to core proportionate calculation approach basis, sales value reference, even minor percentage movements of the royalty may cause greater amount of impact on mining companies as well as for the mid and long term it may hinder mineral sector financial capacity, investment environment as well as competitiveness capacity of the entire sector and country.

Finally, differing positions and arguments of the different state organizations were studied, analyzed and recommendations were provided.

Under this legal study, detailed technical study on exploitation, processing and product production is not considered as well as socio-economic studies, state development and budget policies, in dept numerical analyses and foreign tax regimes are not considered. Some aspects are included in the scope of other expert scope.

Therefore, it is suggested to consider all study reports to be delivered by different experts. In addition, it is noted that conclusions and recommendation made by this report can be changed due to results reached upon conducting detailed studies in those areas.

This study report consists of the following three parts:

1. State Policies,
2. Legal Framework on Royalties,
3. Differing Positions and Arguments of the State Organizations,
4. Conclusions and recommendations.

ONE. STATE POLICIES

Under this chapter state policies on mineral sector were studied, including State Policy on Mineral Sector, Government Action Plan 2020-2024, Long Vision-2050 and State Investment Program 2021-2025 was studied.

1.1. State Policy on Mineral Sector

Pursuant with the State Policy on Mineral Sector approved by the Parliament Resolution No.18 of 2014, following provisions in the Part 2 on ‘Principles to be followed in Mineral Sector’ and Part 3 on ‘Policy Directions for the Mineral Sector’ are stated as relevant with the royalty to some extent:

“Two. Mineral sector principles

2.1. The main principles are defined as follows: to provide sufficient social and economic benefits from mining industry to the public while considering development of the mineral sector and Mongolian National Development Policy which is based on Mongolian Millennium Development goals:

2.1.1. for the purpose of maintaining long-term policy stability of the Minerals Policy to implement principle of **relying on research and study and not to damage stakeholders' legal interest for any decision-making regarding legal framework and tax environment.**

2.1.5. To ensure that the State provides equal terms and conditions for mineral sector investors and not to discriminate by ownership types when implementing "State Minerals Policy";

Three. Policy directions for the mineral sector

3.3. Exploitation industry:

3.3.2. To maximize the state control, regulation and responsibility for the strategically important mineral deposits declared by Resolution No. 27 by Parliament in 2007 to improve their operation and economical benefit and to develop better cooperation between state and private sector.

3.7. Management of mining industry, organization and human resources:

3.7.10. To reduce the exportation of minerals in raw-material form via step-by step measures, support the production of value-added, semi-processed and final products, to support their marketing at international market price, and to improve the estimation methods and methodology for mineral deposit use payment to maximize the income from the mineral industry.”

Considering content of the above-mentioned provisions stated in the State Policies on Mineral Sector, it is concluded that no specific policy directions is reflected with regards treatment of the minor element royalties.

However, as of overall intent of the mentioned provisions, state is willing to improve royalty calculation methods and enhancing economic benefits. It is noted that principle of relaying studies and research results on decision-making for the revision of the tax environment and not harming legal interests of the participants is important for facilitating more balanced and stable environment for the sector and country.

1.2. Government Action Plan for 2020-2024

On 28 August 2020, the Parliament approved the Government Action Plan for 2020-2024 under its Resolution No.24 and following provision is stated as reads to be relevant with the royalty in fiscal and financial scheme of the Part 3 ‘Economic Policy’ of the same plan:

“Three.Economic Policy

...

3.1.10.To support foreign trade by simplifying custom services, protect citizens from an illegal, face products and to continue custom reform to collect taxes on natural wealth fully.”

It shall be noted that it is uncertain whether mineral wealth of the mineral ore, concentrate and products are inclusive under the term of ‘natural wealth’.

Therefore, follow up implementation plan of the same action plan is studied. On 9 December 2020, the Government approved its implementation plan for the Government Action Plan with more detailed implementation measure contents to be taken. However, pursuant with the clause 3.1.10 of the Government Action Plan, implementation measure on royalty was not identified, instead it reflects below content focusing on an improvement of the imported certain goods subject for Excise taxation related programs:

“Based on the e-receipt application used by the citizens smart phones to improve control at all sales stages of all products subject to excise taxation, such as cigarette, alcohol, and improve quality and origin control on medicines, meat and meat products.”

Meanwhile, under the provision 3.2 of the same implementation plan, the Government is planned to improve its deposits with strategic importance regarding mining and heavy industry development, increasing processing level of the commodities and producing value added products as well as establishing oil refinery. Moreover, under the provision 4.5.3 of the ‘Sustainable and unified foreign policy’, the Government is planned to continue protect foreign investor interests and to support reflecting foreign investment, loan with exclusive terms and donations on leading economic sectors, such as mining, energy, food and agriculture and tourism.

In overall, state policy remains focused on facilitating stability of the mineral sector operation and to supporting its development at policy level, but no specific provision was identified regarding treatment of the minor element royalties. In terms of the provision identified potentially relevant to the royalty imposition, no follow up measure was found in its implementation plan.

1.3. Other policy documents

On 12 May 2020, the Parliament approved long term state development policy, so called, ‘the Long Vision-2050’ along action plans to be implemented during 2021-2030. Under the Long Vision-2050, Mongolia defined its ambitious vision to become a leading country with regards to its social development, economic growth and living quality in Asia and it consists of nine sections, including (1) Nations United Values, (2) Human Development, (3) Life Quality and Middle Class, (4) Economy, (5) Governance, (6) Green Development, (7) Save and Peaceful Society, (8) Regional Development, (9) Capital city and Satellite cities.

In the Chapter 4 on Economy, it is planned to improve responsible mining sector and to enhance mineral processing level and capacity and to increase exporting volume during 2021-2030, to develop light and heavy industry, energy sector and construction material production industries as export oriented during

2031-2040, and to straighten shares and positions of its leading economic sectors in global market and to implement diversified economic policies during 2041-2050.

In terms of the five development program to be implemented during 2021-2025 as approved by the Parliament Resolution 24, 2020, under its Chapter 4 on 'Economic Policies', it is planned to export upon adding values by processing major exporting commodities such as coal, copper and iron concentrate, crude oil and with that regards to start construction of the coal-chemical, copper processing and still melting plants along required infrastructure such as railway, water and power supply facilities, immediately.

Remarks

In overall, as per content of the above mentioned most relevant policy documents, the state is aiming to enhance production of the mineral sector, to add values by increasing processing stages and to develop its mineral sector with export orientation.

No specific or particular policy direction or statement was identified with regards to minor element royalty treatment. Even though, custom system improvement measure was identified with regards to increasing tax collection on natural wealth, unfortunately, no detailed implementation measure was spotted as follow up action.

Nevertheless, it is noted that defining principle of relaying on study and research results on decision-making to revise mineral sector tax environment and not harming legal interests of the participants in the State Policy on Mineral Sector is found to be very important in developing more balanced and stable environment for the future development of the mineral sector.

TWO. LEGAL FRAMEWORK ON ROYALTIES

Information on legal framework covering royalty calculation, reporting, payment, and respective methodologies will be addressed based on relevant provisions of the laws and regulations.

With this regard, the Constitution of Mongolia, Law on Subsoil, Minerals Law and respective secondary rules and regulations, General Law on Taxation, Law on Value Added Tax and Law on Investment are studied.

2.1. Constitution of Mongolia

The Article 6 of the Constitution of Mongolia provides legal grounds on ownership of the mineral wealth. On 14 November 2019, such Article 6.2 of the Constitution of Mongolia was revised by the Parliament and become effective starting from 25 May 2020.

“Articles 6

6.1. The land, its subsoil, forests, water, fauna, flora, and other natural assets in Mongolia shall be subject to the people's authority and under the protection of the State.

6.2. The land, except that in private ownership of the citizens of Mongolia, as well as the land subsoil, and its wealth, forests, water resources, and fauna shall be the public property of the State.

The state policy of using natural resources shall be based on the long-term development policy and shall be aimed to ensure the rights for each of current and future citizens to live in a healthy and safe environment, and benefits from subsoil resources shall be accumulated to the Sovereign Wealth Fund and be distributed equally and fairly.

Within the scope of right to live in a healthy and safe environment, a citizen shall have the right to know about environmental impacts of any utilization activities of subsoil resources.

The legal basis to allocate majority of the benefits from utilization of the mineral resources of strategic importance shall be governed by the law in line with the principles that natural wealth to be under people's control.”

Moreover, pursuant with the Article 8.2.4 of the Constitution of Mongolia, the Government is authorized to ‘to protect environment, facilitate rational utilization of the natural wealth and taking rehabilitation measures’ under its common power with regards to managing implementation of the state laws, enterprises, social and cultural sectors.

Subsequently with the recent revision of the Clause 6 of the Constitution of Mongolia, the Ministry of Mining and Heavy Industry is working on revision of the Law on Minerals. On 25 December 202, the working group responsible for such task was established under the order of the Minister for Mining and Heavy Industry. No draft is disclosed yet for the public discussion.

In terms of the taxation, under the Article 7.1 of the Constitution of Mongolia, the Parliament of Mongolia holds power to define state financial, taxation and monetary policies, social development policies, and main directions and to approve Government Action Plan, State Budget and implementation reports as prepared by the Government in compliance with development and national security policies.

Finally, in accordance with the Article 7.1.3 of the Constitution of Mongolia, citizens of Mongolia are obliged to pay taxes imposed by the laws as their core duties.

2.2. Law on Subsoil

This Law is approved in 1988, even prior current Constitution of Mongolia of 1992, and currently its application became quite limited with regards to mineral sector, as detailed schemes on geological study, exploration and exploitation were defined separately by other sub-laws, such as Minerals Law, Law on Petroleum, Law on Common Minerals and Law on Nuclear Energy.

However, with regards to royalty, (1) it provides general legal grounds on having royalty and defining royalty by law and (2) State requirement to capture mineral benefits to the extent possible, by requiring comprehensive study, use of most efficient technology and keeping record of wastes/overburden containing mineral content with economic value and reprocessing them. These are stated in Articles 3 and 11 of the Law on Subsoil as follow:

“Article 3. The subsoil of Mongolia is the property of the State

*The subsoil is the property of the State, in order words, it is the property of all people of Mongolia, in accordance with the Constitution of Mongolia. **The subsoil may be given [to others] only for use.** It shall be prohibited to change the right of the state to own the subsoil.*

Article 10. The purpose of using the subsoil

1. The subsoil may be given for use for the following purposes:

1) conducting geological surveys

2) mining of minerals

3) building and using constructions and structures underground for purposes other than mining, including for storage of oil, gas and other substances and materials; for protecting and burying poisonous substances and industrial waste; and for removing waste water.

4) meeting other needs of companies, organizations and individuals.

2. Issues related to exploration and mining of mineral resources in subsoil shall be regulated by the Law on Law on Minerals.

3. Users of the subsoil shall obtain relevant authorization from possessors and users of land in according with relevant regulations.

Article 11. Fees for the use of subsoil

1. The subsoil shall be used upon payment.

2. The maximum and minimum amounts of fees for use of subsoil shall be determined by the law.”

Moreover, under Articles 31-33 of the Chapter 4 of the Law on Subsoil, regulatory norms, and main requirements of the using subsoil for the mineral exploitation purposes where defined. In particular, Article 31 of the Law on Subsoil defines main principle to conduct exploitation activities based on approved (1) drawings, (2) earth work plans and (3) the technical regulations.

Further, core requirements on exploitation activity were defined under Article 32 of the Law on Subsoil and core principles on mineral processing activity were defined under Article 33 of the same law as follow:

“Article 32. Basic requirements on use of subsoil for mining

The following requirements should be met when using subsoil for mining of mineral raw materials:

- 1) to use methods to extract the core and co-existing minerals, as well as other components efficiently in its entirety and completely;*
- 2) not to create overburden and waste exceeding the determined level, not to exploit selectively only from the content rich parts of the mineral deposits;*
- 3) to conduct comprehensive final and utilization surveys, other geological works, as well as geological and marksheidering activities necessary for use of the deposit; to keep complete technical documentation;*
- 4) to continually account for [the remaining] reserves, changes in reserves, overburden and wastes;*
- 5) not to damage the existing deposits that are being used, as well as any nearby deposits during earthworks, to protect and to store minerals left as reserves;*
- 6) to record and to store production wastes that is mined as by-products and/or none utilized ores containing minerals content which have economic value;*
- 7) to properly use and place the extracted gravel, fertile soil and the overburden;*
- 8) to ensure safety for employees and [local] people, to protect the subsoil, other objects of nature, as well as constructions and structures; to take measures to prevent hazards, to approve and to implement plans on liquidation of consequences of hazards, to rehabilitate the deposit after the end of its use in a way that it can be used for economic purposes.*

Article 33. Basic requirements on processing of mineral raw materials

The following basic requirements should be met during processing of mineral raw materials:

- 1) to use technologies to fully and completely extract valuable components of mineral resources;*
- 2) to record and control the level and amount of extracted components at each state of processing;*
- 3) to further study the composition of the mineral raw material and its technological qualities; to improve the technology;*
- 4) to utilize wastes produced due course of processing of minerals;*
- 5) to record, calculate and protect industrial waste containing valuable components which are not being used.”*

Hereby, it is noted that underlying concept of the Law on Subsoil remains to keep benefits of the mineral wealth to at high level by requiring complete study and use of mineral wealth to the extent possible and to avoid exploiting minerals selectively for high concentrate part, so that less wealth will be disposed as contained in the waste. Moreover, waste contained minerals at certain degree as uncaptured must be recorded.

Besides, under Articles 45-50 of the Chapter 8 of the Law on Subsoil, legal norms and requirements on state mineral wealth registration and record keeping of the mineral wealth balance is defined as follow:

“CHAPTER EIGHT

***THE NATIONAL REGISTRATION OF RESERVES OF
MINERAL RAW MATERIALS, DEPOSITS AND SUBSOIL***

Article 45. National registration of reserves of mineral raw materials and deposits

1. Reserves of mineral resources, deposits and occurrences shall be registered with the central national registry.
2. The national registry of mineral deposits and the national identity of mineral reserves shall be maintained in order to plan geological surveys of subsoil, to determine location for mining plants, to use mineral deposits fully and rationally, as well as for other economic purposes.
3. The registry of mineral reserves, deposits and the subsoil, the registry of mineral deposits and the national identity of mineral reserve shall be maintained by the National Geological Library.

Article 46. The national record of mineral deposits

The national record of mineral deposits should contain information on **the amount and quality of reserves for the core and co-existing minerals, as well as other components**, earth-work machinery, hydrogeological and other conditions for using the deposits, and geological and economic assessments, separately for each mineral occurrence.

Article 47. The national identity of mineral reserves

The national identity of mineral reserves shall contain information on location of deposits whose production is meaningful [feasible], amount of their reserves, their quality, surveying, industrial capacity, mined resources and overburden, as well as amount of geologically surveyed reserves supplied.

Article 48. Determining the level of accuracy of assessment of mineral reserves

The State Geological Library and Information authority shall conduct analysis of accuracy of assessment of mineral reserves, the amount and quality of these reserves, existing conditions, the level of surveying, economic feasibility, and the level of readiness of the deposit for mining and shall determine accuracy of the assessment on the basis of this analysis.

Article 49. Removing mineral reserves from the national identity of mineral reserves

The issue of removing mined minerals, as well as minerals that are turned into unfeasible reserves, reserves wasted during mining, or reserves that were not proven in the course of further surveying or mining shall be decided by the organization that has proven this reserve.

Article 50. The national registry of the subsoil to be used for purposes other than mining

The state central administrative authority in charge of geology and mining shall maintain a registry of subsoil to be used for purposes other than mining.”

It is noted that under the Article 46 of the Minerals Law, the term “**the core and co-existing substitute minerals, as well as other components**” is used to express core and minor elements contained in the mineral ore, concentrate or product.

In overall, Law on Subsoil defines state interest to study and use mineral wealth in its entirety, without wasting any elements contained in soil, including core minerals as well as co-existing or minor elements contained in ore, concentrate or products. However, in terms of the royalty treatment it does not provide provisions on minor elements.

2.3. Minerals Law and Regulations related with the Royalty

Minerals Law

Current Minerals Law has been approved by the Parliament on 8 July 2006 and it was amended number of times during last 15 years. As it amended in 34 occasions, 15 amendments were relevant with the royalty framework at some degree. The major revision was made on 2010, where initially defined simple base royalty scheme of 5% on exported minerals and 2.5% on domestically sold or used minerals was amended with additional comprehensive table of surtax royalty, which would be based on market price and processed levels of the minerals. Also, royalty payment period was shortened from ‘within next quarter’ to ‘within 20th day of following month’ due course.

The main changes occurred as related with the royalty since 2006 is shown in following table:

№	Amendment dates	Content
1	2010.11.25	–Surtax royalty rate table is added. - Government authorized to define Royalty calculation methodologies. -Government authorized to define main principles, methods and requirements on classification of ore, concentrate and product.
2	2011.12.23	– royalty rate on common minerals shall be defined by the Provincial Citizens Representatives Khural within a range between 2.5%-5% and it shall be paid to local budget.
3	2013.10.03	– In accordance with the revised Law on Investment, the royalty shall be stabilized based on Stabilization Certificate.
4	2014.01.24	– Base royalty on gold submitted to the Mongol bank and other authorized commercial banks shall be 2.5% and surtax royalty rate shall be equal to zero.
5	2015.02.18	– Special Royalty rate payable up to 5% as agreed by the parties is defined if State transfers its shares to the private sector and refuses to cooperate on utilization of certain deposit jointly with the private sector.
6	2015.06.04	– Royalty payment period shortened to be paid within 20 th day of the first month of following quarter from the within following quarter.
7	2016.11.10	– Legal framework on ‘derivative deposit’ is defined with the base royalty rate of 2.5% and zero rate on surtax royalty rate, except gold.
8	2019.03.26	– Base royalty rate on gold is increased to 5% with zero surtax rate as submitted to the Mongol bank and other authorized commercial banks. -Royalty payment period further shortened as to be paid within 20 th day of the following month and annual clearance to be made within 10 th of February of the following year. -Royalty resolved not be imposed as duplicative to ore, concentrate and product.
9	2019.11.22	–Pursuant with the Constitutional Court order an Article 47 was revised partially and royalty payer is defined inclusive of person who (1) sold or shipped to be sold, (2) exported, and (3) used for its own purposes. -In accordance with the non-duplicative principle, reported royalty amount on certain mineral by previous seller shall be subtracted from the royalty amount to be imposed on the following seller.

Based on these revisions, it can be concluded that within last 15 years, the legal framework on royalty has become more detailed and sophisticated compared to its initial simple version defined in 2006.

Besides these changes made to the Minerals Law, separate law on windfall income tax of 69% implemented between 2006-201 shall be noted for its negative impacts caused to the county economy, budget, and foreign investment. Please refer to the part 2.7 of this document for detailed information.

Article 47 of the Minerals Law

Main legal grounds on royalties are defined in the Article 47 of the Minerals Law.

Royalty Payer

Under initial version of the Mineral Law as approved back in 2006, the royalty payer was only ‘mineral license holder’, primarily the mining license holder and if exploration license holder used certain amount of mineral for study purposes it required to pay royalty by same rate imposed on mining license holder. Whereas, under current version, as mentioned earlier, irrespective where seller holds mineral license or not, seller and exported shall be the royalty payer.

Royalty Rates

An initial royalty rate consisting of base rate of 2.5% on domestically sold coal and common minerals and 5% on other sold minerals was extended by additional surtax rate on 25 November 2010 differing from the sales value and level processing, divided into the levels of ore, concentrate and products.

However, special rate applies to the gold submitted to the central bank and derivative deposit re-processing activities, which consists 2.5% to 5.0% of base rate and zero surtax royalty rate.

Sales value to be used for a Royalty calculation

As per an initially approved version of the Minerals Law in 2006, the sales value stated to be calculated in order of (1) if exported, the sales value of the product shall be weighted average sales value of the same or similar products as recognized in the international trade in same month (known as monthly reference sales value), (2) if sold in domestic market, then sales price of such product or similar products, (3) an reported sales price by the license holder, if no reference price is available.

Accordingly, under the Government Resolution No.88, 2007, the list international sales value sources for exported mineral products were defined including global commodity exchanges and other sources for types of mineral product. Such principle continues to be applied and as latest version, Government Resolution No.81, 2016 defines list of commodity exchanges and market price sources as below:

Sales value sources	Types of minerals
London Metal Exchange price	Copper, zinc, white lead, black lead, molybdenum
Mongolbank (Central bank of Mongolia) declared price	Gold and silver
Web sources disclosing market value	Iron, coal, fluorspar, permonate ammonia, wolfram, manganese
Sales contract price	Iron and coal (if Sales Contract price is not differing more than 30 percent from the declared “ monthly reference sales value ” declared by Joint Working Group and disclosed by the Mineral Resources and Petroleum Authority web page)

In practice, above mentioned the ‘monthly reference sales value’ or taxable amounts for an exported mineral product are declared by the joint working group established by the Minister for Finance and Minister for Mining (former name) as instructed by the Government Resolution 131, 2013. Such Joint Group is consisting representatives of MOF, MOMHI, General Tax Office and General Custom Office and Mineral Resources and Petroleum Authority.

However, it is noted that further improvement and disclosure is needed as exact methodology on calculating given “monthly reference sales value” is not clear, but seems they are taking weighted average estimation if number of market price in different locations are disclosed by the given web page.

An approach to impose royalty on each and all types of minerals

Phrase to impose royalties ‘to all types of minerals or mineral products’ was stated in an initial version of the Article 47.1 of the Minerals Law as approved by the Parliament in 2006 and still remain reflected in the Minerals Law. Such wording is stated in the following Articles 37.3.3, 47.10 and 47.16 of the Minerals Law:

“Article 47. Royalties

47.3. The royalty rates shall be as follows:

47.3.1. The [base] royalty rate for extracted coal which is utilized for own use, or domestically sold or shipped shall be two and one-half (2.5) per cent of its sales value;

47.3.2. The [base] royalties for gold sold to Mongol bank or commercial banks authorized by Mongol bank shall be five (5.0) per cent of the its sales value and additional surtax royalty rate specified in Article 47.5 of this law shall not apply.

*47.3.3. The [base] royalty rate for **all types of mineral other than those set forth in Article 47.3.1 and 47.3.2 of this law** shall be five (5.0) per cent of their sales value.*

/This section was amended by the law dated 22 November 2019/

*47.10. The payers of royalties specified in Article 47.1 of this law, other than those who sold gold to Mongol bank or commercial banks authorized by Mongol bank, shall pay the royalties within 20th day of next month for **all types of mineral products sold, shipped for sale, or used during the given month** to the state budget and the royalties’ final payment of the given year shall be settled and paid to the state budget within 10th day of February of next year.*

/The numbering of this section was amended by the law dated on 25 November 2010/

/This section was amended by the law dated 4 June 2015 /

/This section was amended by the law dated 26 March 2019/

*47.16. The payers of royalties shall impose royalties on the sales value **for all types of mineral products** as specified in Article 47.7 of this law, without imposing it twice, for the following activities and shall pay it to the state budget.*

47.3.1. sold and shipped for sale;

47.3.2. exported;

47.3.3. utilized for own use.

/This section was added by the law dated 22 November 2019/”

Royalty reporting and payment

Pursuant with the initial version of the Minerals Laws as approved by the Parliament in 2006, an royalty report required to be submitted on quarterly basis and royalty of the same quarter required to be paid within following quarter.

Even though reporting period remained same on quarterly basis during last 15 years, the payment period is narrowed down from quarterly basis to monthly basis. In particular, the royalty of the sold or exported products of the given month shall be paid within the 20th day of the following month.

Classification of the ore, concentrate and product

The classification parameters of the ore, concentrate and product is defined under the “**Key principles and methodology for setting the standards, category and criteria for mineral ores, concentrates and products at the processing level**” is approved by the **Government Resolution No.193, 2011** in accordance with the Article 47.8 of the Minerals Law. An underlying classification criterion of the ore, concentrate or product are mainly based on level of processing and estimated percentage of main minerals contained in them.

However, nothing is found to be noted as how minor elements could impact such classification or even how minor elements contained in certain ore, concentrate or product as supplemental means would be considered and classified.

Regulations on royalty calculation and imposing

Historically, principle of imposing royalty on minor elements based on contained volume of the minor elements in the mineral ore, concentrate and product exported, as tested in by the custom laboratory, used to be defined by the Order A-184, 2010 of the Head of the General Tax Office up until 2019.

Pursuant with the amendments made to the Minerals Law in 2019, on 25 December 2019, the Government of Mongolia approved “Regulation on Royalty Calculation, Imposition, Reporting and Payment” and reinstated such principle of imposing royalty on each of minerals, including minor elements, contained in each ore, concentrate and products, except coal.

Below is the relevant Articles of the “*Regulation on Royalty Calculation, Imposition, Reporting and Payment*” adopted by the Government Resolution N.465 of 2019 on imposing royalties on minor elements, except coal, iron ore and iron concentrate, as per Custom Laboratory testing results.

“Two. Calculating the sales value subject to Royalty

2.1. Sales value subject to Royalty shall be calculated as follows:

2.1.1. sales value of mineral sold, shipped for sale or consumed in the domestic market in a given month shall be determined based on the domestic market price of the product or similar product.

2.1.2. sales value of mineral exported or shipped for export in the given month shall be determined based on the price announced to the public based on the price reference established by the Government under Article 47.2.1 of the Minerals Law;

2.1.3. sales value of gold and silver sold to the Bank of Mongolia and commercial banks authorized by the Bank of Mongolia shall be determined based on the price announced by the Bank of Mongolia on that day.

2.2. If the mineral content of the ore, concentrate, or product differs from the mineral content of the product, the price of which was announced to the public based on the price reference established by the Government, the sales value of the mineral shall be determined on a pro-rata basis according to the mineral content of the product with referenced price.

2.3. The mineral content, percentage, characteristics, and classification of all types of mining products sold in the domestic market shall be certified based on laboratory test results. The laboratory shall be Mongolian or internationally accredited.

2.4. The mineral content, percentage, characteristics, and classification of all types of minerals sold in the overseas market shall be certified based on customs laboratory test results.

2.5. The customs laboratory may use test results of an internationally recognized and Mongolian accredited to issue the certification specified in 2.4 of this Regulation.

2.6. The Customs authority shall deliver the name, type, content, characteristics, and exporter information of the exported mineral to the tax authority electronically in each instance.

2.7. The Royalty shall be imposed on the mineral based on the laboratory test report of the mineral product.

2.8. Sales value of mineral products other than coal subject to Royalty shall be calculated for each base and substitute metal [or minor elements] and mineral product based on the net percentage of the content determined by the laboratory test report.

2.9. Expenses associated with the processing, smelting, refining, and transportation of the product and other operational expenses shall not be deducted from the sales value calculated in accordance with this Regulation.”

Besides on above mentioned Government Resolution, 465, 2019, royalty calculation on coal and iron differs from other minerals as defined per “Regulation on Calculation of the Sales Value of Coal, Iron Ore and Iron Ore Concentrate in Overseas Market for Minerals Royalty Purposes” approved by the Government Resolution N.342 of 2019. The main differences are that realizing ‘contract sales price’ of the exported coal and iron can be used for royalty calculation, subject to up to 30 percent of difference from monthly reference sales value defined by the Joint Working Group and costs incurred up to Mongolian Border checkpoint shall be added to the disclosed contract sales price, if such cost is not included. Main provisions of the same regulation is stated below as:

“Two. Calculation of the sales value of coal, iron ore, iron ore, and iron ore concentrate sold in overseas markets

2.1. The business entity shall calculate the sales value of all types of coal, iron ore, and iron ore concentrate exported and shipped for export in the given month based on the price quoted in the reference price published in databases specified in Annex 2, 4, and 7 of Government Resolution No. 81 of 2016.

2.2. Where a business calculates the sales value of coal, iron ore, and iron ore concentrate exported and shipped for export in a given month subject to Royalty based on the contract price under paragraphs 3 and 6 of the Appendix to Government Resolution No. 81 of 2016, the sales value shall be calculated according to the conditions and requirements specified in this Regulation and submitted to the Tax Authority together with the quarterly and end-of-the-year Royalty Return as well as the information and data specified in the Regulation. This Regulation shall apply to the third quarter return of 2019.

2.3. The sales value of coal, iron ore and iron ore concentrate of an business entity subject to royalty based on the sales contract price shall be determined using the transaction price method specified in Article 17 of the Law on Customs Tariff and Customs Duty on the condition to deliver the products to the Mongolian border station.

2.4. If the following expenses and charges for delivery to the Mongolian border station were not included in the contract price, these shall be added in determining the sales value using the transaction price method specified in 2.3 of this Regulation:

2.4.1. transportation costs;

2.4.2. transportation and export documents related to transportation activities, clearance fees, insurance premiums, and expenses incurred for loading, unloading, storage, and transshipment of goods.

2.5. If the business entity has submitted the mineral sales contract that meets the requirements specified in Article 3 of this Regulation, the information, reports, and documentation specified in Article 5 within the period specified in Article 47.11 of the Minerals Law, the Tax Administration shall verify and finalize the calculation of the Royalties payable by the license holder to the budget based on the sales agreement of the business entity, and validate the Royalties Return.

2.6. If the amount of Royalties calculated by an business entity under Article 2.1 of this Regulation and paid to the budget in the particular month exceeds the amount calculated based on the sale contract price specified in 2.5, the overpaid Royalties shall be refunded or offset.

2.7. If the sales value of coal, iron ore, and iron ore concentrate exported and shipped for export by an business entity determined under Articles 2.3 and 2.4 of this Regulation is less by 30 percent or more than the price announced to the public based on the international market price of the product according to the principle of establishing the monthly average price recognized in the international trade under Article 47.2.1 of the Minerals Law and Article 47.14 of this Law, the sales value subject to minerals Royalty shall be determined as specified in Article 2.1 of this Regulation.”

Royalty reporting forms and templates

Royalty reports are required to be submitted to tax offices as well as special inspection agency on quarterly basis. Therefore, there are two types of form defined by each of the agencies, which are almost same but differs slightly. Royalty reporting forms to the tax authorities is defined by the Order No.A-164 of the Head of the General Tax Office on 30 December 2019, whereas form to be used to the royalty reporting to the specialized inspection agency is defined by the Order A-97 of the Head of the Specialized Inspection Agency on 14 September 2020.

Under those formats reporting is structured to be filled by each types of minerals, but not by the ore or concentrate or product reflecting its content. Therefore, technically, we assume that royalty payers who is reporting minor elements contained in certain ore or concentrate would be filling separate sheet on minor elements as separate type of equal to the core mineral exported but not contained as substitute in certain core mineral ore or concentrate.

2.4. General Tax Law

In accordance with Article 4.1 of the General Law on Taxation, 2019, only Parliament has power to define tax, change, exempt, wave and cancel the taxes, except stabilized taxes applied for the tax stabilization

certificate as per Law on Investment, or tax regimes applied for special trade zones as per Law on Free Trade Zones.

As core classification, Royalties defined under the Minerals Law is considered as official state tax along with the license payments. Moreover, under the Article 9 of the General Law on Taxation, natural wealth, mineral reserves are taxable item and detailed scheme is stated to be defined by specified laws.

Even though, under the General Law on Taxation do not specify, base or minor element royalty matters, it is notable that tax exemption and/or waiver issues are required to be resolved by the Parliament by way of approving specified laws. Meaning that, if royalty regulatory framework to be revised as certain minor elements would be subject to royalty and some would be exempted, or rates would be decreased, or certain costs would be subtracted etc. as per principles of the General Tax Law, such norms are required to be defined under the law. Without any intention, purely for better legal compliance certainty we are stating this.

2.5. Law on Value Added Tax

According to the Article 12.1.7 and 12.5 of the Law on Value Added Tax ('VAT'), the Government is entitled to approve list of final mineral products exported, subject to "0" rate of VAT. Accordingly, under the Government Resolution No.502, 2015, the "List of Final Mineral Product" was approved.

Such list includes, uranium concentrate, molybdenum concentrate, molybdenum oxide, rare earth element concentrates, pure zinc, iron concentrate, purified silver, cathode copper, coal, pure white and black lead and fluorite with technical specifications and custom codes.

It should be noted that Law on VAT and above-mentioned list do not have any differed consideration on substituting minor elements contained in given mineral products. In other words, as per custom codes, it assumed that products are classified as per estimated base mineral percentage contained in the given ore or concentrate.

2.6. Law on Investment

As stated in the Article 4.1 of the General Law on Taxation, under the Law on Investment, both domestic or foreign investors, subject to investment amount and regions invested may apply for tax stabilization certificate, under which main 4 types of taxes, including corporate income tax, customs duty, value added tax and mineral resource royalty, can be stabilized for certain period as defined under the Article 16 of the Law on Investment.

Moreover, under the Article 20 of the same Law, the investor who is to invest more than MNT 500 billion may request and conclude and Investment Agreement, and stabilize its business activity environment, including stabilization of the same four type of taxes. The duration of such Investment Agreement will be not less than period specified under the Article 16 for the tax stabilization certificates.

Meaning that as per Law on Investment, only tax rate of the defined four type taxes can stabilized but potential change in calculation methods, the way of imposing royalties is not included in the term of tax stabilization.

2.7. Other

Law on Tax of the Certain Product Price Increase (Windfall taxation)

Within a scope of this study, the Law on Tax of the Certain Product Price Increase, so called Windfall tax of 68% adopted on 12 May 2006 and terminated by 1 January 2011 is studied as it is relevant with the royalty framework change occurred due course of 4.5 years within last 15 years. Under such law, 68% additional royalty imposed on price increase of the gold, copper ore and concentrate.

Under such law London metal exchange price was used as a reference price and taxable amount for royalty imposition used to be defined after deducting processing cost of USD 850 per ounce of gold price, whereas USD 2600 us deducted as copper smelting cost from each ton of copper ore and concentrate respectfully. Then 68% of windfall tax is used to be imposed.

However, we may note that, notwithstanding, its overall negative impact to the mining industry's foreign investment, performance of the industry, gold supply volume to the central bank etc., exploitation and processing cost of the gold and copper used to be deducted from the sales value in order to define taxable amount for the royalty.

International Treaties

Based on our study no particular provisions found with regards royalty arrangements, specifically, royalty treatment on minor elements, as agreed at by an international treaty level. Theoretically, we assume as matter of taxation rests as matter of sovereignty of the given nations, thus nothing is to be agreed under such instruments.

Remarks

To conclude, main legal framework on minerals is defined by the Minerals Law and respective secondary regulations approved by the Government. Under the Minerals Law, principle to impose royalties on all types of minerals or mineral products is defined with regards exported mineral products and Government is authorized to approve detailed regulations, methodologies with regards royalty imposition and reporting.

However, at law level, meaning under the Minerals Law, no detailed consideration is found on how royalties would be imposed on minor elements which is contained in certain other main mineral's ore, concentrate and product. Instead, requirement to impose royalty on each and all minor elements contained in the minerals or mineral products, excluding the coal, as tested by the laboratory tests is defined under the regulations defined by the Government Resolution No.465 of 2019. Historically, such requirement is used to be applied by the order of the Head of General Tax Office. Therefore, except the coal, all minor elements are subject to royalty as same as core minerals contained in each ore, concentrate or product.

In addition, under currently effective royalty regulation, no exploitation, processing, transportation, and handling costs are allowed to be deducted, instead with regards to iron ore and concentrate, if transportation and handling cost of the iron is not included in the contract price, as to be used for royalty calculation, such cost required to be added on the contract price in order to estimate sales value per DAP-Mongolian border point terms.

Three. Differing Understandings and Grounds of the State Organizations on Minor Element Royalties

On 24 November 2020, the Program arranged virtual meetings between main stakeholders of the matter, including Ministry of Mining and Heavy Industry, Ministry of Finance, General Tax Office, General Customs Office and Mineral Resources and Petroleum Authority of Mongolia and upon taking note of positions expressed by participants their legal grounds were studied accordingly. Consequently, on 25th February 2021, findings were presented to the stakeholders and facilitated discussions.

During the meeting organized we understood that state organizations responsible for taxation and mining matters are having different positions with regards minor element royalty treatment.

The Ministry of Finance relay on Constitutional provisions that minerals or wealth remaining in subsoil shall be in people's consideration and state ownership, therefore, they consider royalty as main mechanism to deliver benefits of exhaustive wealth to citizens. Also, they relay on wordings of the Minerals Law that royalty shall be imposed on 'all types of minerals' and urges that minor elements are considered inclusive in scope a of all types of minerals. In addition, they explained that 65% of the royalty revenue is deposited to the future heritage fund. As main response to the matter, Ministry of Finance hold open position to cooperate if further improvement is needed to make national tax framework more equally applicable and fair, as if globally recognized practice and example exists that exempting or not imposing royalty on minor elements.

The General Taxation Office provided information that as per royalty reporting, currently nine entities are reporting to pay royalty on minor elements, which are relevant to iron, zinc, and copper.

Whereas Ministry of Mining and Heavy Industry insists to relay on types of minerals which are recognized to be economically feasible to exploit and registered in the state minerals funds. They relay on practical concern that if we to impose royalty on each and all types of elements contained in all ore, concentrate and products which will be extinguished or eliminated as waste or slag in further processing and smelting or purification process, then certain deposits will end up becoming uneconomical to mine. Therefore, they insist to study international practice on pricing mineral ores and concentrates, and other country's tax framework and practice, and based on findings proposing to reach common understanding on treatment of minor element royalty.

During the meetings, the mining sector experts of the Program, shared they knowledge and experience with regards pricing approaches in international commodity trade, addressing that certain minerals contained in certain concentrates are usually considered subject to royalty but not all types of minor elements are considered to be subject for royalty, for instance, iron or sulfur contained in copper concentrate are always considered to be uneconomical substance and therefore considered to be none-taxable part, but even at certain degree causes penalty as additional cost and energy or processing stage is needed eliminate them from the core element.

Based on understandings, as of legal findings, following legal observation is made with regards differing positions of the above-mentioned ministries and agencies:

3.1. Ministry of Finance and General Taxation Office positions and grounds

Without ignoring grounds that mineral wealth remaining in subsoil shall be under people's management and state ownership as well as Minerals Law has wording to impose royalty on all types of minerals, based on our findings we suggest following:

1. In accordance with the Law on Subsoil and General Law on Taxation all types of taxes, including royalty, is created by the law and its norms and procedures of how to impose, how to pay and report is also required to be defined by law. Pursuant with such principle and requirement, the way of imposing royalty to all types of minerals can be stated by the Minerals Law in detail, so that no confusing or differing understanding would occur in practices. Meaning that if needed requirements defined by the Government resolution on calculating and defining taxable amount subject for royalty may need to be stated by law, so that tax framework would comply with principle of certainty as per General Law on Taxation.
2. We suggest to study rationality of the approach using unrealized commodity exchange or other reference price for each and all types of minor elements as taxable amount. In this regard, we also suggest clarifying whether value of the elements that would be eliminated or extinguished or wastes as slag during further purification or smelting stages should be imposed royalty. Thus, we suggest considering fairness of imposing royalty on elements contained in certain ore or concentrate but would not bring any economic benefit on their own. Upon study of such matter, principle of exactness would be confirmed so that it complies with reality.

Imposing royalty on economically beneficial minor elements, such as gold and silver, is justifiable, therefore acceptable. However, detailed study is suggested on minor elements that does not bring any economic benefit but would be separated and wasted or extinguished due course of further processing activity.

Moreover, royalty special rate could be considered for minor elements like 2.5% royalty base rate, without surtax royalty rate, for minerals exploited from derivative deposits.

3. The principle of relaying on study and research results on decision-making to revise mineral sector tax environment and not harm any legal interests of the participants stated in the State Policy on Mineral Sector is important in developing more balanced and stable environment for the future development of the mineral sector. With this regard, we suggest to study and access current approach to impose royalty to all types of minor elements by the same rate of core elements based on unrealized reference prices from the angle of tax beneficially principles. Most importantly, we recommend to study mid and long period impact of such strict tax regime on development of the mining sector, its investment environment, production expansion and enhancement level, competitiveness of the Mongolian mining sector, opportunity to introduce new and more efficient technologies as well as impact on tax revenue, state budget etc.

3.2. Ministry of Mining and Heavy Industry positions and grounds

Under the Article 4.1.25 of the Minerals Law, the “reserves of mineral deposit” defined as to be a part of minerals resource which its amount and volume, type, content, and mineral composition are determined in detail by exploration activities, *having economical profit when exploiting by industrial means, and which its enrichment technology and mining-technical conditions of exploitation are determined.*

Further, pursuant with the 48.4 of the Minerals Law, the Mineral Resources and Petroleum Authority of Mongolia decides whether to register certain reserves with Integrated National Mineral Registry, to accept the estimate of reserves and register the feasibility study along with original materials in the database.

However, assuming possible scenario that certain mineral is not captured during exploration stage but revealed due course of the exploitation stages, there are no legal ground to exempt such mineral from

royalty. In other words, as per provisions of the Minerals Law and respective regulations, there is no such legal ground to decide application of the royalty based on its registration record with the national registry.

Notwithstanding, based on our study, in certain country certain ratio or calculation method is used for deduction on certain minor elements as loss to be incurred during its handling and processing. Therefore, besides clarifying on what minor element should be subject for royalty, we suggest also to study pricing practices used in commodity market, tax methods and calculations on defining taxable amount of the certain ore and concentrate including both core and miner elements. Based on such study, grounds, reasons, or rationality of the deductions for certain cost, loss and waste could be clarified and considered for decision-making.

Four. Conclusions and Recommendations

State Policy Documents

In overall, as per content of the above mentioned most relevant policy documents, the state is aiming to enhance production of the mineral sector, to add values by increasing processing stages and to develop its mineral sector with export orientation.

No specific or particular policy direction or statement was identified with regards to minor element royalty treatment. Even though, custom system improvement measure was identified with regards to increasing tax collection on natural wealth, unfortunately, no detailed implementation measure was spotted as follow up action.

However, it is noted that defining principle of relying on study and research results on decision-making to revise mineral sector tax environment and not harming legal interests of the participants in the State Policy on Mineral Sector is found to be very important in developing more balanced and stable environment for the future development of the mineral sector.

Legislations

Under the Article 6 of the Constitution of Mongolia, natural wealth, including the land and its subsoil, stated to be subject to people's authority and shall be public property of the State. Moreover, the state policy of using natural resources declared to be based on the long-term development policy and shall be aimed to ensure the rights for each of current and future citizens to live in a healthy and safe environment, and benefits from subsoil resources shall be accumulated to the Sovereign Wealth Fund and be distributed equally and fairly. Also, legal basis to allocate majority of the benefits from utilization of the mineral resources of strategic importance shall be governed by the law in line with the principles that natural wealth to be under people's control.

On 25 December 202, the working group responsible for preparing revision of the Minerals Law is established under the order of the Minister for Mining and Heavy Industry, but no draft is disclosed yet for the public discussion.

Under the Law on Subsoil, requirements to explore, mine and process all minerals existing in a certain deposit in its natural existence entirety without exploiting selectively are legally defined and provided legal grounds of royalty to be paid against use of subsoil. The maximum and minimum rate of royalty is stated to be defined by the law. Under such provisions of the Law on Subsoil, the terminology 'core and co-existing substitute minerals' is used to consider minor elements contained in an ore.

Whereas, Articles 47, 47² and 47³ of the Minerals Law provides main legal framework on royalties applicable for minerals other than radioactive mineral, oil and gas and common minerals. Even though, under the Articles 47.3.3, 47.10 and 47.16 it is stated that royalty shall be imposed on all types of minerals, there is no detailed consideration on mineral elements contained in certain mineral ores, concentrates and products as substitute element.

Pursuant with the Amendment made to the Minerals Law on 25 November 2010, the Government authorized to approve methodology on royalty calculation and imposition in accordance with the Article 47.6. Consequently, starting from 2011, the Government is approving such methodology up to this date. In particular, first methodology was approved in 2011 under the Government Resolution No.48, later it revised in 2014 under the Government Resolution No.88 and No.220. Currently, 'Regulation on Calculation of the

Sales Value of Coal, Iron ore and Iron Ore Concentrate in Overseas Market for Royalty Purposes' approved by the Government Resolution No. 342, 2019 applies to exported coal and iron and 'Regulation on Royalty Calculation, Imposition, Reporting and Payment' approved by the Government Resolution No.465, 2019 applies to other minerals, including hard-metal minerals.

The requirement to impose royalty on all type of minerals, including both minor elements contained in certain core minerals' ore, concentrate and products based on the laboratory test results is defined under the provision 2.8 of the regulation approved by the Government Resolution No.465, 2019. More precisely, laboratories capable of conducting such test is classified as if such mineral is exported, testing must be done by the Custom's laboratory or equivalent certified internationally recognized laboratory and if such mineral is sold locally then Mongolian certified laboratory could be capable of conducting such testing (provisions 2.3-2.5 of the same regulation).

Pursuant with the provisions 2.8 and 2.9 of the regulation approved by the Government Resolution 465, the sales value of mineral products other than coal subject to royalty shall be calculated for each base/core and side/minor metal and mineral product based on the net percentage of the content determined by the laboratory test report and expenses associated with the processing, smelting, refining, and transportation of the product and other operational expenses shall not be deducted from the sales value calculated in accordance such regulation.

In terms of sales value, as per Article 47 of the Minerals Law and Regulation on Royalty Calculation, Imposition, Reporting and Payment, the sales value subject to Royalty shall be calculated as (1) sales value of mineral sold, shipped for sale or consumed in the domestic market in a given month shall be determined based on the domestic market price of the product or similar product, (2) sales value of mineral exported or shipped for export in the given month shall be determined based on the price announced to the public based on the reference price disclosed by the Government under Article 47.2.1 of the Minerals Law and (3) sales value of gold and silver sold to the Bank of Mongolia and commercial banks authorized by the Bank of Mongolia shall be determined based on the price announced by the Bank of Mongolia on that day.

In other words, as per Government Resolution 81, 2016, (1) the sales value of copper, zinc, white lead, black lead, molybdenum is defined as per London Metal Exchange price, (2) sales value of gold and silver is defined as per price announced the central bank of Mongolia and (3) sales value for of the coal, iron, fluorspar, permonate ammonia, wolfram, manganese is defined by monthly weighted average price of market sources defined by the Government. However, as of exception, contract price of coal and iron is allowed to be used, subject to within 30% difference from the market reference price per DAP Mongolian border port terms.

Historically, above mentioned required to impose royalty on minor elements as per custom's laboratory test, it used to be defined by the Order No. A/184, 2010 of the Head of General Taxation Office between 2010-2019 as guidance or methodology on calculation of the sales value of exported mining products.

Besides this, 'Key principles and methodology for setting the standards, category and criteria for mineral ores, concentrates and products at the processing level' is defined by the Government Resolution No.193 in 2011. Under such criteria, mineral ore, concentrate, and products are classified mainly based on the content percentage of the base or core minerals and nothing is stated with regards minor or substitute minerals contained.

In terms of the differing positions and grounds expressed by main two ministries, Ministry of Finance and Ministry of Mining and Heavy Industry, we have studied legal grounds and provided relevant suggestions with regards reaching common understanding on minor element royalty matters.

In terms of the positions expressed by the Ministry of Finance to rely on wordings of the Minerals Law to impose royalty on all types of minerals without ignoring their grounds, we suggested to study international commodity market pricing principles as well as taxation policies of leading mining countries as well as to initiate comprehensive tax policy study including mining sector economics, its investment environment, competitiveness, and tax efficiency analyses etc. so that rationality of imposing royalty to all minor elements without considering their economic benefits. Meaning that rationality of imposing royalty on minor elements which does not bring any sales benefit but would be wasted, melted out, lost, decreased, or even causes penalty for required additional processing procedures for purification may be questionable to be subject for royalty, since seller would not get any revenue based on those minor elements. As clarification, we do note that minor elements having economic benefit should be continued to be subject for royalty.

With regards to positions expressed by the Ministry of Mining and Heavy Industry, we concluded that as per current legal framework, based on an argument that given minor element is not recorded in an Integrated National Mineral Record or not captured during exploration stage, such minor element could not be exempted from royalty application. Instead, we suggested to conduct specialized study on minor elements from the professional mining and mineral processing industry standpoint to reveal and classify what minor elements should be subject for royalty, but what minor elements should be eliminated as unbeneficial elements which will be wasted, lost, or decreased during further processing stages. Based on those studies, detailed approaches on calculation of taxable amount, loss deduction percentages, sales value defining principles and methodologies could be defined.

Based on this legal study on currently effective legal framework on minor element royalty treatment, we reached following recommendations:

1. Royalty scheme on minor elements better to be defined by the law, as if it will involve certain deductions, exceptions, or special consideration, as those issued mainly defined by laws as tax matter. Having said that, principle stated under the State Policy on Mineral Sector to rely on study and research results on all decision-making processes related with the tax and legal environment of the mineral sector and not harming legal interests of the participants should be properly followed as such approach will facilitate more balanced and stable environment for the future development of the sector and the country.
2. We suggest to undertake comprehensive study on royalty policy, including detailed consideration of the minor element royalty treatment justification, grounds and policies, based on overall impact to country economy, state budget revenue, foreign investment as well as mining sector competitiveness, economy of the mining companies as well as reflecting technical details on what minor element should be considered as beneficial and what minor elements should be taxed with certain deductions or exemptions as certain percentages of those minor elements will be lost or wasted during further handling so that actual realized economic benefit would be decreased or would not be existed at all.

With this regards, Mineral Resources Act 1989 of State of Queensland, Australia¹ and Mineral Resources Regulations 2013 of the State of Queensland, Australia², and other rules, guidelines³ could be considered with regards studying essence of such tax framework and understanding grounds.

¹ Mineral Resources Act 1989, State of Queensland.

² Mineral Resources Regulations 2013, State of Queensland.

³ For example, MRA002.1, Public Ruling-Mineral Resources Act: Determination of Royalty for Prescribed and Special Minerals.

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