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ХУУЛЬ ДЭЭДЛЭХ ЁС

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LEGAL ADVICE AND COMPARATIVE LAW

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1. War of Advice to Transformation Countries and Study of Legal Assistance as an Academic Subject

After the dissolution of the Soviet Union following the revolutions of Eastern Europe, many former Soviet satellite states elected the shift of regime to a capitalist society, rather than maintaining the socialist system. The path these states chose was to reconstruct society by introducing market relationships and thus becoming connected to the rest of the world. As a market system could not have been introduced without building legal infrastructure, many former satellite states asked developing capitalist countries for assistance in building a legal system. Capitalist countries literally competed with each other to transplant their own legal system to these states, because such transplant would enable the country's banks, corporations, law firms, and other entities to secure competitiveness supported by the system. The situation was dubbed a "war of advice" by the media.

Countries providing infrastructure development assistance are constantly exposed to the temptation of using such assistance as a tool to control the economy of the recipient country. That is the reason why, when taking part in assistance, scholars are compelled to concurrently pursue research on issues related to the fundamentals and theories of jurisprudence, which include such questions as: Can law be transplanted in the first place? Why is that justified? What is the best method of legal technical assistance? A notable example is Professor Rolf Knieper, who led Germany's legal assistance. The professor explored methodologies of legal technical assistance through dialogues with scholars of recipient countries, amid tense relationships with legal system implementation work.[1] Scholars' involvement in legal assistance projects has led such assistance itself to be studied as an academic subject, furthering analyses of the universal validity of law across societal and national boundaries, and encouraging study of the context unique to the society of each recipient country. One can say that today's comparative law scholars confront theoretical issues posed by legal assistance that is a hands-on effort.

2. Rationale Justifying the Transplant and Universal Validity of Law

Professor Knieper stands on the recognition that legal universalism, which advocates that law demands its universal validity, is neither an axiom nor a principle with timeless applicability, but a theory that is valid only in a particular phase of the world history—that is, present-day society where capital and labor are invested to produce goods that are traded at markets in exchange for money. A society like this has a structure in which private domains are created through the legitimate pursuit of personal interests

[1] Rolf Knieper, *Juristische Zusammenarbeit: Universalitðt und Kontext* [Judicial cooperation: universality and context] (Wiesbaden: GTZ, 2004); and Knieper, *Rechtsreformen entlang der SeidenstraЯe* [Legal reform along the Silk Road] (Berlin: BWV, 2006).

and supplemented by the public and national domains. In such a society, various principles demand universal validity—including private ownership, the protection of free contract, free business activities, obligation to pay taxes, as well as the principles corresponding to them, such as the nation's obligation to build infrastructure, the government authority's obligation to comply with the rule of law, and the protection of the socially vulnerable—and such universal validity justifies the provision of legal assistance across national boundaries. Accordingly, the purpose of providing legal assistance to a post-regime-change country is not to develop the underdeveloped society, but to help the country fulfill the general duty of developing a legal system in a real-world environment where a society cannot be sustained unless integrated into the global economy through goods and capital transactions. This is predicated on two conditions, one being the existence of a market economy system and the other being need for a legal system in order to maintain markets. In other words, law represents a social relationship that mediates economic relationships of producing and trading goods (i.e., markets), and as such is valid for social relationships in general in a market economy. It can be confirmed that herein lies the rationale justifying the universal validity of law, that from here derives the transplantability of law, and that herein exists the rationale justifying legal assistance.

3. Need for and Methods of Understanding Context

On the other hand, a recipient country's society does not exist as *tabula rasa* or a blank slate on which anything can be drawn; it exists as a society with its own history and unique context. In order for legal assistance to be successful, it is essential to clarify such context and examine over a long period of time the applicability of law to that context. The key is how to reconcile law's demand for universal validity with the context of each country. But, in what method should we understand such context?

A precondition of transplanting law is to link a society to which law is transplanted with the global economy that is based on market mechanisms. Therefore, what is crucial for understanding the society's context is to know what resistance the recipient society may show and what change it may undergo when introducing market relationships and becoming connected to the global market. It is important to pay attention to these points when working to grasp the context of the society.

When examining the best way to build market mechanisms into a society, there are at least two points to consider. The first is how to combine the allocation of social wealth through market relationships with distribution through nonmarket relationships, such as nations and communities. The other is how to arrange the individual components of a market, that is, a place in which transactions are conducted to satisfy demand (buying for use or consumption) and a place in which transactions are conducted to increase value (buying for selling). These two points are likely to be dictated by the society's context, and providing legal assistance without regard to them will probably cause frictions. Even in a society where the majority of social wealth is allocated in the form of articles of commerce, it is not that all the social wealth is commercialized. Each society more or less has its own mechanism by which some categories of wealth are allocated through nonmarket social relationships. A factor instrumental in considering the context of a particular society is what categories of wealth have been allocated through nonmarket relationships or have been subject to restrictions on commercialization. Also, when based on the premise that law represents the very social relationship mediating markets, one can say that forcibly applying law to nonmarket social relationships will cause frictions.

4. Commercialization of Land as a Case Study

(1) Nations' Responses to the Commercialization of Land

Originally, articles of commerce were ones produced by human labor. Land, to which this definition does not apply, has been commercialized through processes unique to each society and nation. Professor Takeshi Mizubayashi, a legal history scholar, defines a historical phase in which land itself becomes an article of commerce as a "society with land market economy," a society with a unique socio-economic structure that is no longer feudalism but is yet to be capitalism.[2]

In China, during the Qin and the Han Dynasties, communities were dissolved and the national system was changed from feudal to province-county one, while land became traded as an article of commerce. These developments triggered the annexation of land and the dissolution of peasantry. However, under the national system of a "society with land market," China adopted the policy of banning the free trade of land to protect small farmers and prevent peasantry from breaking up by prohibiting excessive ownership of land. This policy was clearly aimed at building an equitable society on a national scale. In France, the trend of commercializing land caused each region to codify customary law (law on the recovery of real estate by relatives) in opposition to the trend. At the same time, going against that movement, the theory of contract law was formed within the citizen law system, denying the law on the recovery of real estate by relatives, accepting the commercialization of land, but denying the uncontrolled accumulation of land inconsistent with the principle of justice.

(2) Japan's Experience as a Country to Which Law Was Transplanted

Unlike China, where the commercialization of land was tried to be banned, and France, where commercialization was accepted but purchasing land for selling was legally controlled, Japan's shift from communities to a "society with land market" did not occur spontaneously but progressed in an extremely short period of time pressured by Western powers. For a national system corresponding to this shift, a modern system of absolute ownership was introduced from abroad, which led to the denial of the real-estate redemption system, the denial of the principle of *laesio enormis*, and the approval of trading of land as commercial transactions. As a result, the title to farmland was transferred from the hands of cultivators to the landlord. A parasitic landlord system was established, under which the exploitation of tenant farmers managing farmland became the norm. It was not until the postwar land reform that the government confronted evils resulting from the commercialization of land and succeeded in establishing the land law system as social law to relieve cultivators from such evils. The land reform transformed the economic order of agricultural villages into the one under which the fruits of labor go to farmers. To support this new economic order, the Agricultural Land Act was enacted, abolishing the landlord-type ownership of land that guaranteed the possession of another's labor, and instead introducing farmers' ownership of land based on own labor.

(3) Universal Validity of Law and Context in the Land Law Field

In not a few recipient countries, the main source of social wealth is land (in particular, farmland). Land law is therefore among the legal fields of greatest interest to recipient countries. They have a strong tendency to try to develop the land law system based on the recognition that the way to derive the greatest economic value from land is to immediately privatize

[2] Takeshi Mizubayashi, *Tennosei shiron* [An analysis of the history of the Emperor system] (Tokyo: Iwanami Shoten, 2006).

state- or community-owned land and allow it to be freely traded in markets. Insofar as recipient countries regard land as an investment option, legal technical assistance will be provided to realize the deregulation and liberalization of land transactions. However, Japan's experience as a country to which law was transplanted serves as an eloquent reminder of the consequences such assistance will bring.

As for farmland, it is necessary to start with recognizing that holders of the right to farmland should be the people who have resided and engaged in farming there. The next step has two options: one is to establish the right to farmland only as a use right for the purpose of production; and the other is to establish it as a right that can be disposed of. The appropriate option will depend on the context of the society concerned. When choosing the latter option, i.e., a system that allows farmland to be traded in markets, universal validity should be considered to exist in the legal principle that a person who is responsible for farmland management and resides in that area to engage in farming full-time should become an entity to obtain the right (the concept common, for example, to "Selbstbewirtschafterprinzip(the principle of people producing on their own)" seen in the Swiss law on farmers' land and Austrian state laws concerning the trading of farmland and forests, and to the cultivator principle adopted in Japan's Agricultural Land Act). This will enable the fruits of labor to go to cultivators, while ensuring comprehensive relationships are sustained between producers and land that is the foundation for both their production activities and lives. As a result, land will be cultivated in a manner not exploiting its potential and succeeded to the next generation.

(4) Case 1: Vietnam

Aiming to build market socialism, Vietnam allocated land to farm households by introducing a contract production system, under the framework of advanced cooperatives that were collective farms. This policy was designed to promote a shift from a cooperative-based agricultural production system to a family-based agricultural management system, backed by farmers' dynamism and willingness to engage in production at farms managed personally, not collectively. In other words, the breakup of collective farms was triggered directly by farmers' earnest desire to engage in physical labor and management at the same time. On the other hand, when breaking up collective farms, the land was divided extremely equally, thanks to the communal principle traditional to small villages that had not been completely wiped out even after the formation of socialist collectives. This shows that two trends actually coexisted in the nation's agricultural society, one being the personalization of management, the other being equal allocation of land in accordance with the communal principle. Against this backdrop, the nation's first land law was enacted, recognizing land as a means of production. The 1987 Land Law permitted exclusive use of farmland as a means of production, and disallowed the trading of farmland. Then, the 1993 Land Law permitted land use rights to be traded within the possession limit of three hectares. The land law up to that stage can be said to have been predicated on a farmland market participated by farmers on the basis of a small farmer system. In contrast, developments leading to the 2003 Land Law are seen as having crossed the line of the universal validity principle regarding farmland transactions, not only by enabling farmland to be accumulated via rental transactions over the limit of possession of land use rights and thereby accelerating the dissolution of peasantry, but also by allowing nonfarmer business groups to acquire land use rights. One can say that these measures have been instituted in view of the land market leading to the breakup of the small farmer system.

(5) Case 2: Mongolia

In Mongolia, whose territory was once used almost entirely for nomadic herding, land was not anybody's property but the common asset of which anyone could use any part. However, the nation's shift to a market economy called for non-pastureland to be used for economic purposes in order to help the nation's economic development. This was because there were thought to be no resources other than land that were able to produce economic benefits. Then, to enable land to be freely traded in markets, the government started enacting laws promoting private ownership of land. The first was the Law on Land promulgated in 1994. This law stipulated, first of all, that all the land be owned by the nation, and then that the nation grant it to citizens. The 1994 law, however, did not go so far as to immediately grant land ownership to citizens; instead, it established a scheme under which the nation concluded contracts with private citizens that allowed them to use land for a certain period of time (maximum of 60 years) depending on their purposes. The right granted there was provided for as a possessory right (*ezemshikh*), which was different from ownership. That way, the nation aimed to create an environment where citizens were able to make profits from land, before granting land ownership to citizens by enacting a law permitting private ownership of land (which was realized in 2002).

During the socialist period, farmland belonged to large state-run farms that were managed on a *soum* (district) basis. Privatization of those state-run farms, which covered grain and vegetable production and livestock raising, began in 1991 by way of dividing the production means other than land in the following manner: state-owned property, including state-run farms, was distributed to citizens in the form of vouchers; then citizens joined hands to establish a private company by combining their vouchers. The reason why this method was taken is that, whereas vegetable production could have been managed by family farms, wheat production needed a larger farming scale, requiring the production facilities and machinery corresponding to that scale; and it was not feasible to divide such property on a family basis. It was to those private companies that land possessory rights under the Law on Land of 1994 were granted according to their size. As these rights were not granted to individual farmers, they staged protests with tractors, demanding that the government reallocate farmland possessory rights. In 2003, the government set a 3,000-hectare upper limit on the possessory rights obtainable for land to be used for grain and feedstuff production. As a result, companies possessing land in excess of 3,000 hectares were obligated to return to the government their possession exceeding the limit, and the returned land possessory rights were decided to be granted gratis, preferentially to citizens engaging in farming for five years or longer. The area to be granted was determined to be less than 100 hectares for grain production and less than five hectares for potatoes and other vegetables. In 2008, however, the government reversed its 2003 decision and raised the upper limit on possessory rights obtainable. For land to be used for grain and feedstuff production, the upper limit was raised from 3,000 hectares to 20,000 hectares; and for land to be used for producing potatoes, vegetables, and other plants, the upper limit was raised from 50 hectares to 200 hectares. This decision was made against the backdrop of the emerging situation in which mining and other nonagricultural companies invested in the agriculture business and started operating large-scale farms with tens of thousands of hectares of land.

The Law on Mongolian Citizens Ownership of Land of 2002 introduced private ownership of farmland, which was decided to be granted for a consideration, preferentially to those having farmland possessory rights. In reality, however, private ownership of farmland has not been realized due to extremely high prices. Although granting private ownership of farmland gratis has also been proposed, making it reality will require introducing regulations on farmland transactions at the same time. Such regulations will be needed to ensure that farmland will be owned by local farmers who actually engage in farming full-time and bear responsibility for farm management. On the other hand, as possessory rights are nontransferable, they can be regarded as constituting a legal framework that helps stabilize relationships between farmers and farmland.

While managing grain production in Mongolia does not suit family farms, management through cooperation among residents can be said to accord to the cultivator principle that has universal validity. Therefore, priority should be given to increasing and supporting medium-sized farms managed by local residents, as opposed to nonagricultural entities' mega farms where management and labor are separated and people working there live somewhere else. In the land law field, it is important to provide technical assistance from that perspective.

Under the Constitution, pastureland can be neither possessed nor owned. It is a space open and available to any herder. Nevertheless, the national parliament has recently been discussing a draft Pastureland Law, which is designed to introduce possessory rights to pastureland (especially in suburban areas) and promote settled herding. This movement has been triggered by multiple developments. The first is changing natural conditions under which decreased rainfall has led to deterioration in grass growth. This, in turn, has caused the trend of herders moving to and concentrating in areas with better conditions. Furthermore, with the introduction of a market economy, social infrastructure development projects have focused on the capital and other large cities, causing herders to move to the central area that offers better access to markets. These trends have resulted in an imbalance between the area of meadows and the number of farm animals raised there, creating a vicious cycle by which grass growth has been further hampered. To address the situation, pilot projects have been undertaken by the Millennium Challenge Corporation and other foreign aid bodies, aimed at ensuring the efficient, rational, and sustainable use of grass and encouraging a shift from inefficient nomadic herding to settled herding with higher productivity, by setting areas in pastureland that are exclusively used and managed by particular groups of herders. The draft Pastureland Law is to promote such strategies by establishing a legal framework. Some members of parliament representing *aimags* (provinces) with unfavorable conditions, however, are opposing the draft law. We need to carefully watch how this matter will progress.

For herding in an arid or semi-arid region like Mongolia, the scope of movement is not limited to a certain area, but affected by rainfall as well as natural disasters including snow damage and drought. A pattern of movement is neither fixed nor clear, which inevitably makes boundaries of resource use unclear, too. Groups formed by herders are equally varying, multilayered, fluid, and changeful. Based on such conditions, over a long period of time herders have developed ethics for resource use, including the flexible use of resources and reciprocity (helping each other at times of difficulty), along with social norms dictating pastureland use and its coordination. In the light of such traditional norms gradually losing their effectiveness these days, the proposal has been made to change the form of nomadic herding itself. The issue here, i.e., whether nomadic herding should be extinct or not, is nothing less than a fundamental question about civilization.[3] Even the cultivator principle that has universal validity cannot apply to pastureland as it does not have the historical context of land ownership.

5. A Method of Comparative Law: Comparative "Law and Society"

As discussed above, legal technical assistance that is a hands-on effort calls for scholars of legal theories to take on the challenge of searching for the legal principles that should be universally valid across national boundaries and of analyzing each country's society and its historical context.

Going forward, legal technical assistance is expected to shift its focus from enactment to enforcement of law.

This will likely necessitate long-term joint research projects where the sociology of law will be studied jointly with scholars of recipient countries, and analyses will be made of society's reactions—adaptation, resistance, and rejection—to the law transplanted. What is required of comparative law scholars in the future is to go beyond studying and comparing each country's substantive law and to employ a method of the sociology of comparative law, whereby relationships between law and society as a whole are compared on a country-by-country basis.

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[3] Katsuhiko Tanaka, *Nomonhan senso: mongoru to manshukoku* [Nomonhan War: Mongolia and Manchukuo] (Tokyo: Iwanami Shoten, 2009).

LEGAL REGULATION OF MINING ACTIVITIES IN MONGOLIA: CURRENT ISSUES OF POLICY AND LAW

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1. Introduction

Mongolia is a mineral-rich country landlocked between Russia, China and Kazakhstan. Almost three times the size of France and with a population of only 2.9 million, Mongolia has one of the lowest population of densities of any country in the world. Because of its size and geographical location, Mongolia is hampered by distance from major markets and distance of many citizens from centers of social and economic activity.

The Mongolian economy is dependent on the mining sector and agriculture which have a direct impact, both on economic policy and on the conditions for foreign direct investment. For example, in 2013 the mining sector accounted for over 82.80% of export, 18.50 of GDP[1]. Mining and construction begin only in late March and livestock births peak in the second quarter. There is only a short, single harvest late in the third or early forth quarter.

These factors make Mongolia more vulnerable to external shocks than other transition economies and developing countries. The decline in certain commodity world prices could lead to overspending and high inflation and trigger large swings in real exchange rate that undermine export performance and growth. To avoids this, Mongolia needs to follow expenditure-smoothing policies while actively pursuing diversification. The national mineral policy of Mongolia thus is aimed at increasing the sustainability of mining sector through the promotion and development of export-oriented industries. Consequently, the Government of Mongolia has adopted a number of long-term programs for the exploration of potential mineral deposits, especially of gold, silver and copper since 1991.

[1] N. Algaa. Building a stable legal environment of mineral resources is the basis of economic development. Paper presented to the International Workshop on Legal Regulation of Market Economic Relations: Conflict of Interests and its Consequences. Shikhi Khutag Law School. Ulaanbaatar. 2014. p.140

For the above reasons, the legal regime for mining activities has been developing at rapid pace since the adoption of the existing Constitution of Mongolia in 1992. The Parliamant of Mongolia has enacted laws on land, surface, petroleum, minerals, environmental impact assessment and investments since the adoption of the first Mineral Law in 1994. Mongolia has also enacted legislation dealing with the issue of exploration and mining of radioactive substances. In addition to these legislative acts, the Parliament of Mongolia adopts various policy papers and programmes dealing with the issue of national policies in particular economic sectors. A good example of such policy instruments is the new State Policy in Mineral Resources Sector /2014-2025/.[2]

The new State Policy in Mineral Resouces defines mining sector specific objectives and priorities and its key goal is to accelerate the development of mining industry and increase private sector participation in the Mongolian economy. In this context, the Government identifies private investment as a vital source of much needed capital, technology, management now-how and access to international markets. Foreign investment and direct participation in a wide range of mining related industries are actively encouraged. Such involement is particularly encouraged in connection with the exploration, extraction and processing of mineral resources.

In this article the authors address the issue of the development of mineral policy of the Government of Mongolia, legal regime for mining activities in Mongolia. The authors first describe the role of mining sector in the economic development of Mongolia and then outline the national mineral policy and main provisions of the existing Mineral Law. Also the authors address current issues of mineral policy and law which mining license holders are likely to enter in any Mongolian project.

2. National mineral policy of Mongolia and its implications on the economic development of the country

2.1.The role of the mining sector in the economic development of Mongolia

Up to 1990 Mongolia was integrated into COMECON (Council for Mutual Economic Assistance) markets and the subsidies it received from the former Soviet Union helped to offset its geographical disadvantages. The assistance of the COMECON member-countries had played a vital role in the development of the Mongolian economy. As a World Bank study put it: "From the 1950s until 1990, the Soviet Unoin, along with other CMEA countries, provided a generous volum of financial assistance to Mongolia in the form of grants and low interest loans. Over the second half of the eighties, for instance, foreign source transfers averaged 30 percent of GDP each year. These helped to finance Mongolia's imports of equipment, consumer goods and energy. All the petroleum products consumed came from the Soviet Union, which was also principle purchaser of Mongolia's exports of copper concentrate, wool, leather goods, and meat. Between them the CMEA countries absorbed 97 percent of Mongolia's exports and much of this period , the main transport link with the outside world ran through Western Siberia into the Soviet Union"[3].

Then, however, the economic slowdown and collapse of the Soviet Union and other COMECON countries in the late 1980s and early 1990s brought about a sharp decline and later a virtual cessation of financial and technical assistance to Mongolia. By that time nearly all production and distribution activities were concentrated in large scale state-

[2] The State Policy in the Minerals Sector /2014-2025/ was adopted by the Resolution # 18 of the State Great Hural of Mongolia on 16 January, 2014. www. legalinfo.mn

[3] World Bank, Developing Mongolia, Washington, D.C., 1991, p.1.

controlled monopolies.Consequently, this led to distortions in resource allocation and mounting internal and external imbalances. The early 1990 saw the intensification of social tensions, as shortages of consumer goods became increasingly evident and the country's economy got into a crisis situation. For these reasons Mongolia has experienced an unprecendented decline in real income since 1991. Economic disruptions have included a huge budget revenue loss, severe depreciation of the tugrik resulting from monetary inflation, and a shortage of basic commodities. Also, the shortage of financial resource flows from the former Soviet Union and other COMECON countries has been the essential cause of a sudden interruption of most investment projects, of shortages of key raw materials, petroleum, spare parts, and equipment, and of a sharp drop in consumer goods imports.

At the same time the collapse of Mongolian trade with the COMECON countries, accentuated by a significant deterioration in the terms of trade, has left the country no alternative to expand its economic relations with western countries and attract direct foreign investment. Faced with a sharp deterioration in the macroeconomic picture, the Mongolian Government has taken a series of changes along the lines set forth in the 1991-1993 economic program. Between 1991- 2000 the Government of Mongolia has undertaken a bold reform agenda aimed at stabilizing the economy, strengthening the role of the private sector and increasing the private investment and attracting higher levels of foreign investment to Mongolia. With the support of a broad consensus for its reform agenda, the Government implemented tight monetary and fiscal policies, initiated financial sector reform, eliminated tariffs, introduced a value added tax (VAT) and launched a large scale privatization programme. In particular, the Parliament of Mongolia passed the Mineral Law in 1994. Consequently, the adoption of the new Minerals Law[4] and other commercial laws[5] resulted in considerable progress in macroeconomic stabilization at the end of 1990's.

Since 2000, the Government of Mongolia has continued the measures aimed at strengthening the role of the private sector and improving the environment for foreign investment. Consequently, Mongolia's economic performance has improved gradually, owing to macroeconomic policies. In particular, inflows of FDI have increased gradually since the first revision of the Mineral Law of 1997 between 2000 and 2010.

Despite its isolation and distance from export markets, private investment in the Mongolian mining sector has been dynamic in 2000's. This dynamic has been aided in part by rich natural resources and in part by the mineral legislation and co- production arrangements negotiated by the Government of Mongolia. Consequently, creating the conditions to attract foreign mining companies[6] to the mining industry and to improve Mineral Law have been important components in national mineral policy and structual

[4] The first Mineral Law was replaced by the secont Mineral Law in 1997. For this issue see "Introduction to Mineral Resources Law"(2012), National Legal Institute of Mongolia, Anand Batzaya advocates, Ulaanbaatar, pp 14-19

[5] For example, the Foreign Investment Law was adopted in 1993. For an overview of the development of the Mongolian foreign investment legislation see I.Idesh "Impact of International Law on the Development of the Mongolian Investment Legislation and Its Legal Consequences" (2012), Materials of International Workshop on Trends of the Development of International Law in Mongolia, School of Foreign Service of the National University of Mongolia, National Intelligence Academy, National Legal Institute of Mongolia, Ulaanbaatar

[6] Mongolia acceded to the WTO in 1996 and the Government of Mongolia complies with trade related investment measures (TRIMS) that specifically prohibits requirements, for example export performance or local content requirements. Issues of obligations and commitments of the Government of Mongolia before the WTO are not considered in detail within the framework of this article.

reform since 1990. As a result of such foreign investment policy and mineral law reform in Mongolia, the mining sector has become a major contributor to the national economy and mineral policy of the Government of Mongolia has played a core role in the Mongolian economic development. Therefore, the next section addresses the policy issues relevant to the mineral resources sector and mining activities.

2.2. Overview of the recent mineral policy of the Mongolia and its implications on the economic development of the country

As we have briefly noted in the previous section of this article, in order to create favourable conditions for mining activities and promote foreign direct investment the Government of Mongolia has devoted considerable resources to the development of its mineral legislation since 1990. The first sources of mineral legislation to be considered is the Petroleum Law of Mongolia, adopted in 1991, which introduced to Mongolian law a new type of agreement "production sharing agreement". The next important legislative act which gave direction to the further development of mineral legislation was the Mineral Law of Mongolia of 30 September 1994 ("the 1994 Mineral Law). This Law introduced a concept of strategic minerals and contained detailed provisions on mining licenses, tender bidding and license fees and legal status of state administrative organs in charge of mineral policy.

Following the adoption of the 1994 Mineral Law Mongolia's economic performance not only improved but also led the Government to take a series of economic measures. The Government implemented tight monetary and fiscal policies, initiated financial sector reform, eliminated tariffs, introduced a value added tax (VAT) and launched a large scale privatization programme. The Parliament of Mongolia thus passed the new Mineral Law in 1997 with a view of mainly facilitating foreign direct investment and creating more jobs. Among its provisions, the Mineral Law reduced the rate of royalties from mineral production by 10 percent. The new rate was established at 2.5 percent.

These actions resulted in considerable progress in the effectiveness of the activities of mining companies and and inflows of FDI have been increased in 2000's. The strong presence of the mining sector in FDI can be explained in part of the mineral law reform of the Government of Mongolia in this period. In particular, separate laws dealing with varoius issues of mining activities including appropriate legislation on licensing of economic activities, taxation and environmental impact assessment have been enacted or amended. The Mineral Law of 1997 was also revised in 2006 ("the 2006 Mineral Law). This act introduced a concept of investment agreement and regulated various issues of the development of exploration and mining projects and environmental aspects of mining activites. The 2006 Mineral Law has also taken into account the Constitution, other legislative acts in force such as the Surface Law, Petroleum Law, Land Law, Foreign Investment Law and other laws. Following the adoption of the 2006 Mineral Law, the Government of Mongolia has declared several mines including Oyu Tolgoi as a deposit of strategic importance. The Investment Agreement between the Government of Mongolia and Ivanhoe Mines and Rio Tinto plc for Developing Oyu Tolgoi Gold- Copper Project was signed in October 2009.

But Mongolia's national policies on foreign investment and mineral resources and mineral legislation have been sharply affected by a number of domestic and international developments since 2009. The adoption by the Parliament of Mongolia of the Law on Regulaion of Foreign Investments in the Economic Sectors of

Strategic Importance[7] and other laws[8] was met with strong opposition from foreign and domestic investors in Mongolia. The sharp decline in the government revenues from state owned mining companues which produce copper, coal, and iron has placed pressure on the Government of Mongolia to institute compensatory measures since 2012. These measures not only included increases in rate of royalties and the introduction of minimum cost of exploration but also led to the revision of the 2006 Mineral Law and adoption of the new State Policy in the Mineral Resources Sector in July, 2014 .

Thus, the legislative framework for mining activities has expanded quickly over recent years and Mongolia has adopted a comprehensive Mineral Law and other laws which belong to different branches of law. The next part of this article deals with the general legal framework for mining activities in Mongolia.

3. Legal framework for mining actvities in Mongolia

The rules of public and civil law which have been specially established for mining activities apply to mining companies in Mongolia. Among such rules, the 2014 Mineral Law which regulates various issues of the development of exploration and mining projects and environmental aspects of mining activites is a key source of mineral legislation in Mongolia.

As we have noted in the previous part of this article, Mongolia last revised its Mineral Law in July, 2014 and the existing Mineral Law,[9] sets forth the general principles of the legal regime applicable to mining activitites and mining companies[10]. The existing Mineral Law has the following chapters:

Chapter One – General Provisions;

Chapter Two – State Regulation in Minerals Sector;

Chapter Three – Prospecting and Exploration of Minerals;

Chapter Four – Mining of Minerals;

Chapter Five – Conditions for Maintaining Eligibility to Hold a License

Chapter Six – Obligations of a License Holder;

Chapter Seven – Transfer and Mortgage of Licenses;

Chapter Eight – Termination of Licenses;

Chapter Nine – Information, Royalty Revenue Distribution, Reimbursement and Specifics of Finance and Accounting;

Chapter Ten – Resolution of Disputes Arising in Connection with Licenses;

Chapter Eleven – Liabilities.

The 2014 Mineral Law has 66 articles and covers various issues of the development of exploration and mining projects such as the ownership of mineral resources, mining licenses, transfer and pledge of licenses, termination and revocation of licenses, environmental protection and mine closure[11]. Below is

[7] This Law restricted foreign direct investment in certain sectors of the Mongolian economy and then was replaced by the Investment Law of Mongolia in 2013.

[8] The laws which have prohibited to grant exploration licences were adopted in 2011, 2012 and 2013.

[9] Complementary provisions of mineral law are found in other laws and regulations (such as environmental law, foreign investment regulations). For example, legal aspects of land use and environmental protection are regulated by the Land Law and Environmental Impact Assessment Law of 2001. However, these issues are not considered in detail within the framework of this article.

[10] At present, Mongolia has adopted separate laws on petroleum and radioactive substances which more typically regulate relations in the petroleum and nuclear energy sectors and not mining. The Petroleum Law was adopted in 1991 and last revised by the Parliament of Mongolia in July, 2014. Issues of importation, production, sales and transportation of petroleum producs are regulated by the 1995 Petroleum Products Law. The Law on Nuclear Energy was adopted in 2009. This Law contains provisions that apply to mining and enrichment aimed at the production of uranium and thorium. However, the issues of exploration and mining of oil and uranium are not considered in detail within the framework of this article.

[11] Majority of provisions of the 2006 Mineral Law bearing the state regulation in minerals sector, pow-

a brief summary of the main provisions of the existing Mineral Law.

Purpose of the Law. The purpose of the Mineral Law is to regulate the prospecting, exploration and mining of mineral resources and protect the environment[12]. The concept of mineral is defined in Paragraph 4.1.1 of Article 4 of the Mining Law as any usable natually occuring concentration that was formed on the surface or in the subsoil as the result of geological evolutionary processes[13].

Ownership of mineral resources. Legal aspects of ownerhip of natural resources are regulated by the Constitution of Mongolia[14], Land Law, Mineral Law and other laws[15] and all minerals resources occurring on and under the earth's surface in Mongolia are the property of the State. The 2014 Mineral Law does not restrict foreign investment in exploration and mining license holders. However, this Law imposes requirements for state equity participation in mining license holders and the State may own up to 50 percents of participating interests in a private legal person.[16] The State may also own up to 34% of the shares of an investment to be made by a license holder in a mineral deposit of strategic importance when its proven reserves have not been determined by the means of state budget funded explorations.

Exploration and mining licenses and eligibility of license holders. Exploration and mining license holders must be Mongolian legal entities and only an exploration license holder is entitled to apply for a mining license in the exploration licensed area pursuant to Article 24.1 of the Mineral Law. Exploration licenses are issued for a period of three years. An exploration license holder has the right to obtain three extentions of the term of an exploration license for three years pursuant to Paragraph 1.5 of Article 21 of the Minearl Law. Exploration license holder has priority rights to apply for and obtain mining licenses provided that such legal persons satisfy the requirements set forth in the Mineral Law[17]. The criteria to which the granting of an exploration license has to be refused are contained in

ers of state administrative agency and local administrative agencies, procedures for submitting application to issue licenses, procedures for submitting application to extend the term of exploration and mining licenses and obligations of license holders have been preserved in the existing Mineral Law.

[12] See Article 1 of the Minerals Law of Mongolia . www.legalinfo.mn

[13] Provisions of the existing Mineral Law don't apply to petroleum, natural gas, radioactive substances and common minerals. See Article 3.1 of the Mineral Law. The Common Minerals Law was adopted in January, 2014.

[14]The Constitution of Mongolia provides expressly that land, underground resources, air and water are object of exclusive ownership by the people of Mongolia. See Article 6.1 of the Constitution of Mongolia. The Land Law provides for ownership of land by Mongolian citizens and the State. See in detail the Land Law of Mongolia www.legalinfo

[15] Foreign nationals including foreign investors are not permitted to own land. The same prohibition applies to legal entities, whether Mongolian, foreign or jointly owned. Foreign mining companies in Mongolia are limited to acquiring land possession and use rights. However, they may own property constructed on the land such as building, factories, warehouses and other structures. See Article 12.1 of the Investment Law of Mongolia. The amended Foreign Investment Law of 1993 was replaced by the Investment Law in 2013. Investment Law of Mongolia. www.legalinfo.mn

[16] This provision applies only to minerals deposits of strategic importance where such deposits have been discovered by the means of state funded exploration works. See Article 5.4 of the Minerals Law of Mongolia

[17] In addition to this right, an exploration license holder has the following rights under Article 20 of the Minerals Law:

1. to conduct exploration for minerals within the boundaries of an exploration area;
2. to transfer the exploration license under the terms and conditions of this law or surrender all or part of the exploration license area with the permission and under supervision of respective authority;
3. to have access to the exploration area and construct temporary structures with the purpose of conducting exploration work;
4. to pass through the land surrounding the exploration area for the purpose of entering the exploration area;
5. to enter and pass through the land owned or possessed by other persons.

Paragraph 2.1 of Article 19 of the Mineral Law. This is especially the case when the application and the attached documents fail to meet the requirements set forth in the Mineral Law.

Mining licenses are issued for a period of 30 years. A mining license holder has the right to extend the term of the mining license two times for a period of twenty years each depending on the reserve of the mineral[18]. The criteria according to which the granting of a mining license has to be refused are contained in Article 26.3 of the Mineral Law. This is especially the case when the application and attached documents fail to meet the requirements set forth in the Mineral Law.

Transfer and pledge of licenses. The Mineral Law provides for the transfer of exploration and mining licenses with certain restrictions. An exlporation license holder may transfer its license to another legal person eligible to hold the license only after providing evidentiary proof that the materials and reports on prospecting and exploration work have been sold and taxes have been paid. A mining license holder may transfer its license after providing evidentiary proof that the mine together its machnery, equipment and documents have been sold and taxes have been paid. The Mineral Resources Authority records the transfer of license within five business days following the receipt of the transferor's application. Pledging of licenses is also allowed and issues of pledge agreement are regulated by the 2014 Mineral Law. Exploration and mining license holders may pledge their licenses to any banks or non-banking financial organisations with a view of financing their investments and mining projects.

Termination and revocation of licenses. Licenses may be terminated[19] and revoked under grounds set forth in the Mineral Law. In particular, licenses may be revoked by the Mineral Resources Authority on the following grounds pursuant to Article 56 of the Mineral Law:

1. The license holder has failed to meet the general requirements for mineral exploration and mining operations;

2. The license holder has failed to pay the license fees within the specified period;

3. An exploration area or a mining area has been designated as special purpose territory and the license holder has been fully compensated;

4. The exploration expenditures of the particular year are lower than the minimum cost of exploration set forth in Article 33 of this Law;

5. The State central administrative agency in charge of environment has decided, based on a report of the local administrative bodies that the license holder had failed to fulfill its environmental reclamation duties.

Environmental protection. License holders may only start their operations on receipt of permit from an environmental

[18] In addition to this right, a mining license holder has the following rights under Article 27 of the Minerals Law:
1. to engage in mining of minerals within the mining claim;
2. to sell mineral products and minerals extracted from the mining claim at international market prices on foreign markets;
3. to conduct exploaration for minerals within the mining area;
4. to transfer and pledge all or part of the mining license pursuant to procedure set forth in this Law;
5. to enter and pass through the mining area, construct necessary structures and use the mining area in order to carry out mining activites;
6. to pass through the land adjacent to the mining area;
7. to enter and pass through the land owned or possessed by other persons as approved by the owner or possesser of the land in order to exercise the rights provided by this Law;
8. to use land and water in compliance with applicable laws.

[19] Pursuant to Article 53 of the Minerals Law, licenses may be terminated in the following cases:
1. expiration of the license term;
2. surrender by the license holder of the entire licensed area as set forth in Article 54;
3. revocation of the license by the state administrative agency.

authority. An exploration license holder must prepare an environmetal protection plan. An exploration license holder has to submit its environmental protection plan to the governors of soum or district where the exploration area in question is located. An exploration license holder also has to deposit funds equal to 50 % of its environmental protection budget for that particular year in a special bank account established by the Governor of the relevant soum or district. Where a license holder fails to fully implement the measures set forth in its environmental protection plan, the Governor of the relevant soum or district may use such funds to implement these measures and the license holder in question has to provide additional funds required for doing so.

A mining license holder must assess environmental impacts and prepare an environmental management plan. The objective of environmental assessment procedure set out in the existing Mineral Law and Environmental Assessment Law is to promote the identification, assessment and consideration of environmental impacts of the proposed mining activites. Among its provisions an environmental management plan provides measures aimed at protecting air, water, humans, animals and plants from various adverse impacts of the mining operations.

A mining license holder has to submit its environmental impact assessment and environmental protection plan to the state central administartive organ in charge of environment. A mining license holder has to deposit funds equal to 50 % of its environmental protection budget for that particular year in a special bank account. Where a license holder fails to fully implement the measures set forth in its environmental protection plan, the state central administartive organ in charge of environment may use such funds to get involve professional organisations to perform the relevant reclamation works and the license holder in question has to provide additional funds required for doing so.

Mine closure. A mining license holder has to inform the state central administrative organ in charge of environment of its intention to close its mine or mining operations at least one year prior to such closure. A mining license holder has to take all necessary measures to ensure safe use of the mine area for the further public purposes and reclamation of the environment. It also removes all machinery, equipment and other property from the mining area. Mining license holders have to prepare a detailed map showing dangerous or potentially dangerous places created by mining operations and submit such map to the professional inspection agency and the local Governor.

Therefore, the Mineral Law is a key source of mineral legislation and contains detailed provisions on all phases of mining activities and rights and obligations of license holders and other stakeholders. However, the existing laws, governmental acts and decisions of government agencies contain serious violations of the Mineral Law and human right legislation[20]. These problems usually exist in the relationship with mining license holders and foreign mining companies. In particular many issues associated with administration of laws, license fees and royalties remain uncertain and unstable[21].

[20] Kh. Selenge. " Obligation and Responsibility Before Economics: Issues of Theory and Practice" (2013), Law Review Journal, Law School, National University of Mongolia, Ulaanbaatar. p.15

[21] There are 39 mining regulations and procedures which have been adopted by the Ministry of Mining, Ministry of Energy and Mineral Resources Authority of Mongolia as of 1 December, 2014. These rules and procedures regulate such issues of mining activities as the safety, open pit operations, issue of mining licenses, submission of information and reports to the Mineral Authority and other government agencies and other issues of mining operations. For example, it is necessary to change the Implementing Rules of the Mineral Law, adopted by the order of the Chairman of the Mineral Resources Authority # 133 of 17 December, 2001 since the activities of mining companies are affected by these Rules. Therefore, it

Certain current issues of mineral policy and law of Mongolia thus are addressed in the next part of this article.

4. Current issues of mineral policy and law of Mongolia

As we have described in the previous part of this article, Mongolia has adopted a comprehensive Mineral Law setting out the legal regime for mining activities. The 2014 Mineral Law regulates various issues of the development of exploration and mining projects such as the ownership of mineral resources, mining licenses, transfer and pledge of licenses, termination and revocation of licences, environmental protection and mine closure. Domestic and foreign investors may obtain exploration and mining licenses. The mining license entitles the holder to exploit the extractable minerals found in the mining area and conduct ore prospecting in the mining area. Mining license holders may also export to foreign markets their mineral products and minerals extracted from the mining claim. These legal guarantees exist in the context of the current legal regime for mining activities and thus the 2014 Mineral Law provides a liberal regime.

Although the importance of the mining sector is growing for the economic development of Mongolia it should be noted that the on-going businesses and mining operations do cause damage to the Mongolian people's health and environment. As of 2011, 17000 hectares have been exploited for mining activites in 15 provinces of Mongolia and only 5000 hectares of land have been reclaimed[22]. Besides that more than 1000 hectares of soil have been damaged because of the so called artisanal mining operations[23]. In particular large coal and iron projects are causing a considerable damage to the local people and herders who lose their paster land and water resources. For these reasons, various civil society organisations have emerged at the end of 2000 and they are now invlolved in various legislative drafting activites and even have certain arrangements with the main Mongolian political parties and movements[24].

Thus, the mineral legislation of Mongolia still is developing under the conditions of a harsh struggle between various public groups, political parties and movements. For example, in the Mongolian parliament there are still diametrically opposed approaches to solving problems of right of ownership of land and surface and principles of state regulation of the economy and mining concessions. That's why only certain provisions of the Mineral Law of 1997 were amended or modified respectively in 2006 and 2014. These provisions which mainly regulate license fees and royalties and seriously affect the economic and financial activities of mining companies.

is necessary to pay attention to the present practice of government agencies in charge of environment, mining and geology. However, these issues of mineral law are not considered in detail within the framework of this article.

[22] M. Enkh-Amgalan "The Resource Sector in Mongolia: Is It Time for Mongolia to Consider Embracing FSIs? Is Production Sharing Agreement a Better Option for Mongolia?" (2013-2014 /03/), Mongolian Law Review Journal, International Law Committee, Mongolian Bar Association, Ulaanbaatar, p.60

[23] In Mongolia issues of artisanal mining operations are regulated by the governmental act and this current issue of mineral policy attracts the interests of lawyers and legal scholars. For this current issue of mineral policy and law see P. Munkhselenge "Legal issues in the Mining Sector of Mongolia" (2013-2014), N 03, Mongolian Law Review Journal, International Law Committee, Mongolian Bar Association, Ulaanbaatar. However, environmental aspects of mineral legislation of Mongolia are not considered in detail within the framework of this article.

[24] A good example of this kind of arrangement involving political parties and civil society groups are the last two revisions of the the Minerals Law of 1997. On the participation of civil society organizations in the mineral legislative drafting see in detail . N.Algaa, Building a stable legal environment of mineral resources is the basis of economic development. Paper presented to the International Workshop on Legal Regulation of Market Economic Relations: Conflict of Interests and its Consequences. Shikhi Khutag Law School. Ulaanbaatar. 2014. P. 134- 138

License holders have to pay license fees annually pursuant to Article 32 of the Mineral Law. In addition to that the 2014 Mineral Law introduces a concept of minimum cost of exploration and royalties. An exploration license holder thus has to perform exploration works with expenses not less than the amounts specified below per hectar of the license area pursuant to Article 33.1.1 of the Mineral Law:

1. US$ 0.5 for each of the second and third years of the term of the exploration license;

2. US$ 1 for each of the fourth to sixth years of the term of the exploration license;

3. US 1.50 for each of the seventh to ninth years of the term of the exploration license.[25]

A mining license holder has to pay the state budget royalties based on values of all products extracted from mining claim or sold or shipped for sale or mined[26]. That's why the 2014 Mineral Law introduces a new concept of export control over minerals extracted from the mining area. This new control was met with strong opposition from foreign and domestic investors in Mongolia since the 2014 Mineral Law increases the cost of transactions and production expenses of license holders.

But the adoption of the 2014 Mineral Law is not accompanies by the adoption of the corresponding implementation rules and procedures concerning minimum cost of exploration and royalties. At the same time the Parliament of Mongolia intends to make amendments and modifications to the existing Mineral Law and other laws soon[27]. Besides that the third Chapter of the State Policy in the Minerals Sector 2014 provides that the State will improve the legislation dealing with the issues of transfer of exploration and mining licences, transfer of shares of mining license holders and gold export control.[28]

Certainly Mongolia needs to amend the existing Mineral Law and other laws regulating environmental issues and other

[25] Article 32.2 of the Minerals Law provides that exploration fees are payable for each hectar at the following rates: US$0.1 for the first year, US$ 0.2 for the second year and US$ 0.3 for the third year of the term of the exploration license ; US$ 1.00 for each of the fourth to sixth years of the term of the exploration license; US$ 1.50 for each of the seventh to ninth years of the term of the exploration license. In respect of mining area, US$ 15.00 are payable for each hectar under Article 32.3 of the Minerals Law.

[26] Pursuant to Article 47.2 of the Minerals Law such values are determined as follows:
1. In respect of products which have been exported, values are determined on the basis of international market prices of such products or similar products and these prices are determined on the basis of recognised principles of the average monthly calculation methodology of international trade;
2. In respect of products sold or utililised on the domestic market, values are determined on the basis of the domestic prices of such products or similar products;
3. In respect of products which have been sold on international and domestic prices, market prices are determined on the basis of sales revenue which have been declared by a license holder where it is impossible to determine such prices.

[27] At present the working group of the Ministry of Industry has prepared a new draft of Trade Law which provides that a mining companies may ship its export products only after the relevant advance payment has been transferred into its bank account in Mongolia and the permit to ship the minerals to foreign markets has been given to such mining company by the customs office in question. In my opinion, this law draft is aimed to increase the powers of some government agencies such as the Mineral Resources Authority, General Customs Department and other inspection agencies. Therefore, various negative legal consequences of provisions concerning export controls found in the existing Minerals Law and other acts are to be researched with a view of improving the Mongolian mineral legislation in future.

[28] The current issues of mineral policy and law also include such issues of mineral legislation as the human rights, environmental protection and public participation.However, these issues are not considered in detail within the framework of this article. For these issues see I.Idesh "Issues of Public Participation in the Mining Projects" (2013), N4, Law Review Journal, Law School, National University of Mongolia, Ulaanbaatar, Materials of Workshop on International Law and Challenging Issues of Mining Sector , 14 June, 2013, Foreign Service School, National University of Mongolia, National Intelligence Academy, National Legal Institute of Mongolia, Ulaanbaatar

current issues of mineral law mentioned in Chapter 3 of the State Policy in the Mineral Resources Sector in the nearest future. In this connection it should be noted that first of all, the most important issues of mineral policy and law such as the minimum cost of exploration and calculation of royalties pursuant to Article 47.2 of the Mineral Law are to be researched with a view of avoiding various negative legal consequences of export control over the economic and financial activities of mining licenses holders.

5. Conclusion

The development of the Mongolian mining sector has been dynamic since 1991. This dynamic has been aided in part by rich natural resources and in part by the mineral legislation and co-production arrangements negotiated by the Government of Mongolia. One of important components in national mineral policy and structual reform has been and still remains is to create more liberal legal regime for mining activites in Mongolia. Mongolia last revised its Mineral Law and other laws regulating various mining activities in July, 2014 to that effect. The new State Policy in the Minerals Resources Sector (2014- 2025) which provides a more comprehensive and long – term approach to mining sector policy formation and implementation has also been adopted by the resolution # 18 of the State Great Hural of Mongolia in January 2014. Despite the last revision of the Mineral Law and other laws, Mongolia still needs to amend certain provisions of the existing Mineral Law dealing with the issues of transfer of exploration and mining licences, transfer of shares of mining license holders and gold export control in future.

Certainly, some of these challenging issues will be met with the strong opposition from many civil society organisations and political movements. In our opinion, this legal uncertainty may cause various negative legal consequences in practice since the 2014 Mineral Law applies to the ongoing businesses and foreign investment mining projects in Mongolia.

Therefore, Mongolia needs to have a stable national policy in the mining sector since this sector is crucial to the future economic growth of Mongolia. In order to attract investments more successfully to the mining sector in Mongolia investments do have a greater need for stability than other short term industrial projects. In this connextion it is necessary to establish a stable legal environment for mining activites because many current issues of mineral policy and law remain uncertain.

Finally, it should be noted that the creation of a stable legal regime for mining activites is impractible without a well-thoughtout national mineral policy that is supported by guarantees to domestic and foreign investors set forth in the legislation. Consequently, first of all it is necessary to research such challenging issues of mineral policy and law of Mongolia as the transfer of exploration and mining licences, transfer of shares of mining license holders and gold export control in the context of the improvement of mineral legislation of Mongolia in future. For this reason, the authors propose to study the mining codes and regulations of some extractive industry dependent countries and to amend the most important aspects of the 2014 Mineral Law.

INVESTMENT ENVIRONMENT OF DEVELOPING COUNTRIES DEPENDENT ON EXTRACTIVE INDUSTRIES – THE FATE OF MONGOLIA?

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1. Race to the top or race to the bottom?

With the opening of borders since the beginning of the globalization era, the mobility of goods, services, capital and labor, which enhances the possibility for corporations to shift between countries, has led to competition between countries at the international level. This reduction in border controls has brought more sharply into focus the ways in which differences in national arrangements including regulatory systems, may act as 'non-tariff barriers' hindering cross border flows.[1]

Regulatory competition can be described as the process in which regulators deliberately engage in the provision of a more favorable regulatory environment in order to attract the benefits associated with corporate activity.[2] The theory implies companies' power in shaping the governments' regulatory policy directly or indirectly. This idea of private entities exercising power over the state is controversial itself; however it is a well-documented fact of the political economy.[3]

Regulatory competition theory assumes that companies have some choice as to what regulatory law will govern their activities and where they will locate their activities. Different states' corporate law and tax law, as well as other regulations, apply varying bases for prescriptive jurisdiction, and accord varying degrees of choice to companies.[4] However, the threat of relocation is not the only way companies can influence the state; they have the following options in regard to a potential change in regulations[5]:

- relocate production to a new location;
- lobby, educate, and litigate regulations that reflect their interests;
- mutually accept whatever regulations come their way.

Over time, the preferences of firms will shape state regulations.[6] Governments respond to firm behavior, as they balance the interests of their constituencies and their own interests. There is opportunistic competition among governments, as with firms. Government can:

[1] William W. Bratton, Joseph A. McCahery, Sol Picciotto& Colin Scott, *Introduction: Regulatory Competition and Institutional Evolution,in* International Regulatory Competition and Coordination, Perspectives on Economic Regulation in Europe and the United States 1 (William W. Bratton, Joseph A. McCahery, Sol Picciotto& Colin Scott eds., 1996).

[2] See generallyid.

[3] See generallye.g. Joe S. Bain, Barriers to New Competition (1956); F. Modigliani & M. Miller, The Cost of Capital, Corporation Finance and the Theory of Investment, 48(3) Am Econ Rev 261–97 (1958); Mancur Olson, The Logic of Collective Action (1965); Alfred D. Chandler with the assistance of Takashi Hikino, Scale and Scope (1990).

[4] Joel P. Trachtman, International Regulatory Competition, Externalization, and Jurisdiction, 34 Harv. Int'l L.J. 47, 60 (1993) (citation omitted).

[5] Dale D. Murphy, The Structure of Regulatory Competition: Corporations and Public Policies in a Global Economy 10 (International Economic Law Series, 2004).

[6] See generally e.g. JOE S. BAIN, BARRIERS TO NEW COMPETITION (1956); F. Modigliani & M. Miller, The Cost of Capital, Corporation Finance and the Theory of Investment, 48(3) AM ECON REV 261–97 (1958); MANCUR OLSON, THE LOGIC OF COLLECTIVE ACTION (1965); ALFRED D. CHANDLER WITH THE ASSISTANCE OF TAKASHI HIKINO, SCALE AND SCOPE (1990).

- unilaterally relax regulations to lower production costs for domestic firms (deregulation);
- exert pressure on foreign countries to change regulations (influence, diplomacy);
- erect regulations that protect domestic firms against foreign rivals.[7]

However, there can be other forms of competition among states through measures such as the circumvention of existing laws and regulations. This can be done through the creation of special economic zone[8] or by offering legal protection to investors through bilateral investment treaties and state contracts.[9] Some scholars even argue that competition pushes states to relax enforcement of the existing laws and regulations.[10]

The first model of this theory was introduced by Charles Tiebout who argued that the promotion of competition between local governments should lead to an optimal balance between the level of taxation and the provision of public goods.[11] According to his theory, rational individuals being informed of available choices will choose the preferred location of specific public goods and a local public goods equilibrium can be established if local governments use their offerings to attract citizen to their territory.

The theory has evolved considerably since then and has been applied in many different contexts with several refinements and been applied to diverse subjects. Because of the fact that the theory of regulatory competition has been developed in the United States on the basis of federalism, its assertions were first applied in the American context. Nevertheless the lessons learned from its application in the American context are relevant at the international level[12] despite the differences of political and institutional contexts, though these do present complications[13].

It is, however, questionable whether one can simply extend theTiebout model to the international level and conclude that regulatory competition produces an efficient equilibrium.[14] The efficiency properties of international regulatory competition depend on the absence of both market and political failures. The preconditions for efficiency are rare, even in integrated markets. As Radaelli has stated, 'It is hard to find regulatory domains with full factor mobility, adequate and symmetrical knowledge of the characteristics of different jurisdictions, the possibility of preventing other jurisdictions from successful innovative regulatory policies, wide choice of destination jurisdictions, economies of scale, and jurisdictional latitude in the selection of regulatory laws'.[15]

Hence the debate on regulatory competition at the international level is less interested in the efficiency properties of the equilibrium and more interested in

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[7] Id.

[8] See Krishna ChaitanyaVadlamannati, Race to the Top or Race to the Bottom? Competing for Investment Proposals in Special Economic Zones (SEZs): Evidence from Indian States, 1998–2010 (working paper, 2011), available at http://www.uni-heidelberg.de/md/awi/professuren/intwipol/top_bottom.pdf (last visited April, 19, 2012).

[9] See Kyla Tienhaara, Mineral Investment and the Regulation of the Environment in Developing Countries: Lessons from Ghana, 6 IEAPLE 371 (2006).

[10] Eric Neumayer, Greening Trade and Investment: Environmental Protection Without Protectionism 148 (2001).

[11] See generally Charles Tiebout, A Pure Theory of Local Expenditures, 64 J Polit Econ 416 (1956).

[12] See generally supra note 7. See alsoSimon J. Evenett& Robert M Stern, Systemic Implications of Transatlantic Regulatory Cooperation and Competition (2011).

[13] See generally Yves Dezalay, Between the State, Law, and the Market: The Social and Professional Stakes in the Construction and Definition of a Regulatory Arena, inInternational Regulatory Competition and Coordination, Perspectives on Economic Regulation in Europe and the United States 60 (William W. Bratton, Joseph A. McCahery, Sol Picciotto& Colin Scott eds., 1996).

[14] *See generally* John D. Wilson *Capital Mobility and Environmental Standards: Is There a Theoretical Basis for a Race to the Bottom?in*Fair Trade and Harmonization: Pre-Requisites for Free Trade? 393 (Jagdish Bhagwati & Robert Hudec eds., vol I, 1996).

[15] Claudio M. Radaelli, The Puzzle of Regulatory Competition, 2, 24 JNL. PUBL. POL.1 (2004).

the direction of regulatory races. Theories concerning regulatory competition disagree about what can be expected from the interaction between governments and markets in regulatory policy. Distinct theories were born with 'notions of 'races' to the 'top' and to the 'bottom'[16] in the academic discussion, and these offered us bewildering conclusions on the consequences of regulatory competition.

Many support international regulatory competition as a necessary tool to create businesses and jobs by creating regulations that are more efficient and less expensive which will benefit the overall economy of the host country. They argue that regulatory competition can be important as it reduces the regulatory costs imposed on companies, which will be passed further on to consumers. Different localities' desires to attract businesses will spur governments to devise regulations that are efficient and find new ways to improve older regulations.[17] This is labeled a 'race to the top'[18].

In the meantime, many scholars have raised the criticism that international regulatory competition lessens the sovereign capacity of states to regulate corporate behavior. More importantly, they argue that the enhanced mobility of companies puts them in a position of bargaining power, and they don't hesitate to use this advantage to extract regulatory concessions from host governments. These concessions may often not be favorable to social welfare, especially in the area of environmental protection of the host country. Due to corporate migration in response to looser regulations, states will have no choice but to refrain from adopting socially optimal regulations. Corporations may engage in regulatory arbitrage, playing off one government against others. This effect is called the 'race to the bottom'[19] theory in which 'states are rendered helpless in countering the effect of heightened corporate mobility'.[20]

However, both theories have conventional aspects which are perceived as problematic and which offer their own complications. There is little agreement on the assessment of risks associated with economic activity, the assessment of the costs and benefits that would result from restrictions, or the preferences for levels and types of regulation.[21] In short, neither of the theories dominate.

2. Structure of regulatory competition

The 'race to bottom' or 'race to top' theories are not necessarily mutually exclusive. It is impossible to argue that one theory is utter rubbish and other is absolutely accurate. Rather it is safe to say that either a race to top or a race to bottom occurs depending on the circumstances.

The direction of the race depends on the differing private sector interests and state responses to them. Companies interact in the context of specific economic conditions when calculating the cost and benefits of their regulatory choices.[22] Murphy has outlined the structure of regulatory competition in terms of determining this direction. According to him, the outcome of the race depends on three related propositions:

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[16] *SeeId.*, at 4.

[17] See Jennifer Smith-Bozek, Regulatory Competition: A Primer 1 (2007), available at http://cei.org/pdf/6319.pdf (last visited April, 19, 2012).

[18] *See generally* DYNAMICS OF REGULATORY CHANGE: HOW GLOBALIZATION AFFECTS NATIONAL REGULATORY POLICIES (David Vogel, Robert Kagan eds., 2004).

[19] This term was introduced by Cary *in* William L. Cary, *Federalism and Corporate Law: Reflection upon Delaware*, 83 YALE L. J. 663 (1974). *See also* Ralph K. Jr. Winter, *The "Race for the Top" Revisited*, 89 COLUM L REV 1526 (1989).

[20] *See generally* RICHARD J. BARNET & RONALD E. MULLER, GLOBAL REACH: THE POWER OF MULTINATIONAL CORPORATIONS (1974).

[21] See generally Radaelli, supra note15.

[22] *See generally* Eric Brousseau& Fares M'hand, *Incomplete Contracts and Governance Structures,in*INSTITUTIONS, CONTRACTS AND ORGANIZATIONS: PERSPECTIVES FROM NEW INSTITUTIONAL ECONOMICS, (C. Menard, ed., 2000). *See also* Klaus Dieter Wolf, Nicole Deitelholf, & Stefan Engert, *Corporate Security Responsibility*, 42 Journal of Cooperation and Conflict 294, 299-300 (2007).

- Process regulations versus market access regulations;
- Industrial structure;
- Specificity.[23]

a. First proposition- Process regulations versus market access regulations

The first proposition implies a state's choice of restriction based on production or market access. States may limit or prohibit manufacturing or service industry processes within their jurisdiction. These are called 'process restrictions'. Or they may restrict the market access of particular services or products. These are called 'market access restrictions'.[24]

Process restrictions restrict the way in which a good or service is produced. Without regulations, firms would generally seek the lowest cost method of production; hence process regulations are likely to increase the cost of production. Domestic business and labor in a state with costly restrictions on manufacturing processes tend to operate at a disadvantage with respect to competitors in less highly regulated countries.

In the absence of common international action for a common higher standard, both export oriented and import competing sectorial interests will fight for lax national restrictions to improve their competitive position. In the case of costly regulation or inexpensive relocation, firms may move to less highly regulated countries. The threat of industrial relocation and the result of loss of jobs and tax revenues many convince governments to keep process standards lax.

Market access restrictions, for their part, are perceived as a form of protectionism for domestic businesses. Restriction on market access is an effective barrier to entry against competitors. Domestic business and labor may push for a market access restriction to the extent that it reflects their interests and in the absence of common international action against market access restrictions as de facto trade barriers, sectorial interests may seek to impose domestic product regulations that improve their competitive position.

b. Second proposition - Industrial structure

The second proposition is industrial structure. This proposition enhances the strength of the market-access-process proposition. Powerful firms influence states to achieve regulations that reflect their particular interests. This influence can be direct, indirect, or even imputed by governments.[25] Firms' power may stem from their revenues, employment, market share, control of the media, personal or historical ties to top state officials, access to information, national security or industrial policy relevance.

Concentrated markets facilitate collective action and the ability to shape regulations. Oligopolies have a greater chance of achieving their regulatory goals through lobbying, litigation, education, and advertising.[26] Also they have asymmetrical access to information; indeed they are often the only source of detailed information to regulators. States are most likely to respond to powerful firms both as a result of lobbying pressures and to improve their own political survival by boosting employment and economic growth.

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[23] See Murphy, *supra note 5* at 11.

[24] According to Murphy, this distinction is adapted from the traditional product-process distinction. *See* Murphy, *supra note 5. See also e.g.* Michael Porter The Competitive Advantage of Nations (1990); David Vogel, Trading Up: Consumer and Environmental Regulation in the Global Economy (1995);Craig Murphy, International Organization and Industrial Change (1994); Anthony Ogus, Regulation: Legal Form and Economic Theory (1994); Peter P. Swire, *Symposium on Constructing New Federalism: Jurisdictional Competence and Competition: The Race to Laxity and the Race to Undesirability*, 14 Yale J. on Reg. 67 (1996).

[25] *See* Murphy,*supra note* 5, at 4.

[26] *See id.* at 42.

c. Third proposition- Specificity

Specificity can include a whole range of different factors. The investments may include human, dedicated, physical, brand, and site specificity.[27] However, site/asset specificity is most important in international cases. Asset specificity means 'durable investments that are undertaken in support of particular transactions, and that would lose considerable value if the transaction were prematurely terminated'[28]. There can be three types of asset specificity: low, international and domestic.

Low asset specificity means that assets can be easily redeployed. Firms with investments with low asset specificity may relocate to less restrictive regulatory environments. These firms have greater mobility. Low asset specificity facilitates a competition in laxity in which moves by one state to attract or keep industry through lax heterogeneous regulations are matched by other states.

High asset specificity can occur both on the international and domestic levels. Domestic asset specificity occurs when assets are specific to transactions in one country. Firms with investments specific to transactions only in the domestic market fight against regulatory homogeneity that threatens their investment. They support heterogeneous regulations that protect their investment.

When asset specificity is international, the firm's assets are specific to transactions in more than one country. This includes assets dedicated to particular export markets or dedicated to greater production than the domestic economy can absorb, as well as foreign direct investments and other cross border transactions. Firms with assets devoted to cross border transactions seek regulatory homogeneity on issues that affect transaction costs. Firms oppose divergent regulations that inhibit the effective use of those assets and increase transaction costs. Investments with high multinational asset specificity create incentives for firms to push for common regulatory outcomes across borders.

According to Murphy when asset specificity is high, firms need a more complex structure to ensure credible commitments and continuity. He argues that a movement away from lax heterogeneous regulation toward stringent homogenous regulation is analogous to a movement away from market contracting and toward a unified structure and that more homogenous regulations act to harmonize contracts.[29]

This structure of regulatory competition is helpful to see clearer picture and gives us a chance to apply it on the countries with dependency on extractive industry. In the following section, I will try to apply the structure of regulatory competition on the countries that are dependent on extractive industry and identify the direction that the theory implies.

3. Applying the propositions of regulatory competition in developing countries dependent on extractive industries

As I have briefly noted in the introduction, the investment climate comes second when it comes to deciding where to invest in the extractive sector. Only after countries offer similar geological conditions may competition be based on other factors such as infrastructure, access to foreign markets, the investment environment and so on. As Omalu and Walde have stated, 'any country with a favorable geology has to combine this with an attractive mineral investment regime to attract considerable mineral sector investment.'[30]

[27] *See generally* OLIVER E. WILLIAMSON, ECONOMIC INSTITUTIONS OF CAPITALISM (1985). *See also*, Oliver E. Williamson, *The New Institutional Economics: Taking Stock, Looking Ahead*, 38 JEL 595 (2000).

[28] *See generally* OLIVER E. WILLIAMSON, ECONOMIC INSTITUTIONS OF CAPITALISM (1985) *id.*

[29] *See* Murphy, *supra note*5, at 35.

[30] See M. K. Omalu, T. Waelde, Key Issues of Mining Law: A Brief Comparative Survey as a Background Study for the Reform of Mining Law, 3-13 CEPMLP (1998), available at http://www.dundee.ac.uk/cepmlp/journal/html/vol3/article3-13.html (last visited March, 13, 2012).

In this section, an overview of extractive industry dependent developing countries will be given. Against this background, general assumptions will be made and the propositions of regulatory competition will be applied.

i. Overview

In a number of low-income, mineral-rich countries extractive industries can represent a considerable share of overall FDI entering the country, and can contribute significantly to state revenue. These countries have few other industries that can attract significant FDI due to their small domestic markets and weak production capabilities and FDI in extractive industries is deemed to be the most important.

These countries are referred to as 'extractive industry dependent' countries. The World Bank, in its report, used standards of the average annual export value of oil, gas, or mineral products exceeding 15 percent of total exports to determine what constitutes an extractive industry dependent country.[31] T

he World Bank found that there were 20 oil and gas dependent countries and 30 mining dependent countries in 2007.[32]

Another study shows that between 1996 and 2010, the number of low and middle income countries that depend on minerals increased by more than 30 percent from 46 to 61 countries. By 2010, more than 80 percent of non-fuel, mineral-dependent states was low- and middle-income countries, compared to about 70 percent of fuel-dependent countries.[33]

Since 2005, more than 75% of non-fuel, mineral-dependent countries have become more dependent on minerals. In 14 of those countries, mineral dependence has increased by more than 25 percentage points since 2005. In Burkina Faso, for example, the mining sector accounted for 2% of exports in 2005, but by 2010 its share had risen to 41%. Over the same period, the relative size of the mining sector in Laos more than doubled from 17% of exports to 45%.[34] More and more low and middle income countries have become extractive industry dependent due to the price boom since 2005.[35]

In these countries, the relative importance of foreign companies in production varies. Foreign affiliates account for from fifty percent to up to virtually one hundred percent in most of the countries in the non-oil and gas industry.[36] In oil and gas industry, there is a wide variation; while in west Asia foreign affiliates' output amounted to an average of only three percent of production, in sub-Saharan Africa it amounted to 57 percent on average.[37]

Both governments' policies and TNCs' investment decisions are influenced by the volatility of mineral markets. Governments actively seek ways to attract foreign investors while MNCs seek natural resources. Studies found that around 120 countries have reformed their legal regimes for mining since 1985.[38] Structural adjustment programs aimed at shifting the mineral sector to the private sector which were developed by the World Bank/International Monetary Fund played an important role in this field. And at the

[31] *See* OED, OEG & OEU, *supra note* 2 at X. This standard has been chosen with reference to the WBG's Poverty Reduction Sourcebook, which states, "A country's mining sector can play an important role in poverty reduction strategies if the approximate share of the mining sector is…greater than 10–25 percent of export earnings…."

[32] For a list of countries meeting this criterion, *see* UNCTAD, *supra note* 1, figure 4 at 125.

[33] See generally Dan Haglund, Blessing or Curse? The Rise of Mineral Dependence Among Low- and Middle-Income Countries, Oxford Policy Management Report (2011), available at http://www.opml.co.uk/sites/opml/files/OPM%20Blessing%20or%20curse.pdf (last visited June, 20, 2012).

[34] Id., at 3.

[35] Id.

[36] *See* UNCTAD, World Investment Report 125 (2007), figure 4, at 125, available at http://unctad.org/en/docs/wir2007_en.pdf (last visited July, 20, 2012).

[37] See id., figure 5, at 126.

[38] *See generally* JAMES OTTO & JOHN CORDES, THE REGULATION OF MINERAL ENTERPRISES: A GLOBAL PERSPECTIVE ON ECONOMICS, LAW AND POLICY (2002).

turn of the millennium, more and more geologically interesting countries with acceptable legal and fiscal frameworks became available to international investors.[39]

MNCs have been the most important players in the global mineral market since as early as the beginning of the twentieth century. MNCs are typically originated from international industries where there are high barriers to entry and deploy in domestic markets in developing countries and economies-in-transition. In 2003, according to the World Bank, the non-fuel extractive industry was dominated by some 50 major mining and metals companies operating globally and by origin these were concentrated in four countries: the United States, South Africa, Australia, and Canada. The large scale mines of those companies generated about eighty five percent of the world's whole production of nonfuel minerals.[40]

Countries that depend on either non-fuel or fuel minerals are also more likely than other countries to suffer from institutional governance problems such as corruption and political instability. The Transparency International Report shows a high correlation between corruption and the dominance of extractive sectors[41]. Moreover, Haglund found that there is a negative correlation between institutional development as measured by the World Bank's Worldwide Governance Indicators, and countries that are dependent on either fuel or non-fuel minerals. In other words, mineral dependence tends to be associated with poor institutional governance.[42]

Overall, the increased number of countries that have become dependent on extractive industry and increased competition among developing countries for extractive industry investment are evident and there exists a negative correlation between dependence on extractive industries and host country's institutional governance.

Against this background, the following assumptions are crucial for applying the structure of regulatory competition to extractive industry dependent countries.

ii. Assumptions

In order to apply the propositions of regulatory competition, general assumptions have to be made. FDI mobility, the occurrence of competition only amongst developing countries, host governments and their political elites' rent seeking behavior are the main assumptions.

For the developing economies that are dependent on extractive industries, the assumption of corporations being mobile is most likely only in the case of MNCs. Because of the fact that local businesses tend to have stronger connections to local markets and less possibility or capability to change legislation, the discussion mainly focuses on MNCs which possess greater mobility.

Also, it has to be clear that we are assuming that regulatory competition occurs only between developing countries and not between developed and developing countries. As Porter claims the policies of all countries may not be equally affected by the constraints of international competition and the problem is not the

[39] John P. Williams, *Legal Reforms in Mining: Past Present and Future, in* INTERNATIONAL AND COMPARATIVE MINERAL LAW AND POLICY, TRENDS AND PROSPECTS 37, 38 (E. Bastida, T. Waelde, J.Warden-Fernandez, eds., 2005).

[40] Monika Weber-Fahr, John E. Strongman, RamaniKunanayagam, Gary McMahon & Christopher Sheldon, *Mining,in* THE WORLD BANK, MACROECONOMIC &SECTORAL APPROACHES 440, 441 (vol 2, 2003).

[41] *See generally* Carlos Leite & Jens Weidmann, *Does Mother Nature Corrupt? Natural Resources, Corruption and Economic Growth* (IMF working paper, 1999) (arguing that natural resource abundance creates opportunities for rent-seeking behavior and is an important factor in determining a country's level of corruption), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=259928*(last visited March, 20, 2012)*; Transparency International, *Corrupt Political Elites and Unscrupulous Investors Kill Sustainable Growth in its Tracks, Highlights New Index,* press release, Berlin (2002). The index rated 26 of 32 mineral-dependent countries as corrupt or highly corrupt.

[42] *See* Haglund,*supra note* 33, at 4.

existence of a 'race to bottom' in relatively rich countries. The negative impacts of competitiveness concerns are to be found in relatively poor nations, many of whom have been reluctant to enforce their environmental standards out of fear that their economies will suffer a competitive disadvantage vis-a-vis other relatively poor nations. The regulatory standards of these countries, he claims, are "stuck at the bottom." Thus, they are "dragging down" the regulatory standards not of rich countries but of other poor ones.[43] We may also exclude some cases where the country's mineral dependency is based on domestic corporations.

In the regulatory competition debate, the assumption is often made that there is full democracy. However, when there is a clear negative correlation between mineral dependency and institutional governance, the rent seeking behavior of government elites or political figures should be included and it should be accounted for as an important factor.

iii. Applying the propositions

When the theory on the structure of regulatory competition is applied to developing countries dependent on extractive industries several observations can be made which are laid out in the following subsections.

Process restriction versus market access restriction

In terms of process regulations versus market access regulations, there are several factors that make market access restrictions less important in the extractive industries of developing countries.

First, developing countries lack the financial capital, technology and knowledge resources to extract non-renewable natural resources.[44] Few countries, especially among developing countries have or are able to obtain the resources needed for such investments, and the sheer scale of the projects frequently requires MNCs to co-invest.

Second according to some scholars, the global regime governing investment rests broadly on a principle of 'the more the better' in terms of FDI.[45] The perception that an increase in FDI might trigger renewed protectionism has led to some concern. However, this trend appears to be confined to a relatively small number of countries. In 2006, 147 policy changes making host-country environments more favorable to FDI were observed.[46]

Third, domestically rooted mining companies generate only a small portion of the world's total mineral production. Developing countries seem to care more about making the market more accessible and focus on FDI since domestic companies mostly operate in small scale mining and provide relatively small revenue to countries' economies.

In terms of environmental protection, access restriction becomes important in terms of the 'pollution halo' or 'California effect'[47]. It is based on Porter's hypothesis suggesting that stronger environmental policies can improve competitiveness in

[43] Gareth Porter, *Trade Competition and Pollution Standards: 'Race to the Bottom' or 'Stuck at the Bottom'?*, 8 (2) JED 133, 138 (1999).

[44] UNCTAD, *Transnational Corporations, Extractive Industries and Development: Implications for Policies* 9 (2006), *available at* http://archive.unctad.org/en/docs/c2em20d2_en.pdf *(last visited March, 20, 2012).*

[45] Lyuba Zarsky, *From Regulatory Chill to Deep Freeze?*, 6 IEAPLE 395, 396 (2006).

[46] Torbjorn Fredriksson, *Transnational Corporations, Extractive Industries and Development (UNCTAD)*, 4(3) ATDF 41, 41 (2007).

[47] The California Effect offers a model of firm behavior that is predicated on the existence of relatively large, highly regulated markets in the world's richest countries. Firms seeking to export to these markets must meet the latter's relatively strict environmental and consumer standards. Having been forced to adjust their exports to meet these standards, it is then in their interest to have their home country adopt similar standards, since this enables them to achieve better economies of scale by producing more similar products. Higher regulatory standards may also give them some advantage vis-a-vis domestic competitors who haven't geared up to meet the standards of stringent regulation countries. Further, *see* David Vogel & Robert A. Kagan, *National regulations in a global Economy*, in DYNAMICS OF REGULATORY CHANGE: HOW GLOBALIZATION AFFECTS NATIONAL REGULATORY POLICIES 6 (2002).

the marketplace by fostering innovation and efficiency, therefore attracting investors. However, this theory cannot be applied to developing countries, because it can only be applicable in cases where domestic political or economic pressures in a country with stringent environmental regulation targets the environmental practices of a particular sector of a less 'green' country, where countries with production aspire to enter into 'green' country markets, or the production is covered by an effectively enforced multilateral environmental agreement.[48] Also this only works in an industry that produces a homogenous product with little customer or brand name loyalty[49].

In extractive industries, process restriction is more relevant for the following reasons. First, extractive industries are heavily regulated. These industries usually need more-than-usual involvement of the state in the licensing of mining companies, the regulation of the sector, and fiscal and financial matters, including taxation, fees, and investments in supporting infrastructure. Even though, starting from 1980s, privatization of state owned assets to foreign investors and the adoption of legal frameworks that are more investor friendly in developing countries has occurred, extraction industries remain regulated.

Second, process restriction is also important because the extractive industry is a high footprint industry which has an enormous impact on the host country. The often substantial fiscal incomes derived from mining can lead mineral-dependent economies on a cycle of corruption and inefficient governance. At the same time, a dominant mining sector can lead to Dutch disease[50] effects on the non-mining economy, endangering the promotion of other sectors.

The environmental impacts are also overwhelming; emission is not the only pollution problem in extraction industries; habitat destruction, water pollution, water quantity loss, biodiversity loss, noise, dust and other upstream problems (land and ecosystem degradation, acid drainage, slop failures, etc.) are the predominate concerns[51]. These issues also adversely affect food security and the health and livelihood of the poor and vulnerable groups with little mobility or means of alleviating negative impacts.[52] Mining projects are often located in remote areas where indigenous communities are members of a distinct cultural group, often a minority within a community of minorities. Here, mining activities can have a negative impact on the livelihood of indigenous people, especially with regard to issues concerning land tenure, often causing socio-cultural conflicts within and between communities.

Since it is now evident that process restriction is more relevant to extractive industry, we now turn to an analysis of process restriction in the case of developing countries.

The process restriction proposition implies that in the case of high process restrictions, the cost of production is likely to be higher than the cost of

[48] *See generally* David Vogel, *Environmental Protection and Economic Integration, (*Prepared for a Workshop on Regulatory Competition and Economic Integration: Comparative Perspectives, Yale Center for Environmental Law and Policy, 2002) *available at* http://iatp.org/files/Environmental_Regulation_and_Economic_Integrat.pdf*(last visited March, 13, 2012).*

[49] *See* Otto & Vogel, *supra note* 38, at I-41.

[50] The Dutch disease hypothesis is that a positive shock (boom) to an important primary product causes an appreciation of the real exchange rate. This results in a movement of resources to the non-tradable and the boom sectors and away from tradable manufacturing and agricultural products. The exchange rate shifts can cause problems in promoting competitive diversification into non-commodity sectors. *See* in Monika Weber-Fahr, John E. Strongman, RamaniKunanayagam, Gary McMahon & Christopher Sheldon,*supra note* 40, at 465.

[51] ALYSON WARHURST, ENVIRONMENTAL DEGRADATION FROM MINING AND MINERAL PROCESSING IN DEVELOPING COUNTRIES: CORPORATE RESPONSES AND NATIONAL POLICIES 41 (OECD, 1994).

[52] *See* Monika Weber-Fahr, John E. Strongman, RamaniKunanayagam, Gary McMahon & Christopher Sheldon, *supra note* 40, at 443.

productions in less highly regulated countries. Businesses in a state with costly restrictions on processes tend to operate at a disadvantage with respect to competitors in less highly regulated countries.

As discussed in the previous section, when there is no international agreement to set a common higher standard, export oriented extractive industry interests will fight for lax national restrictions to improve their competitive position. In the case of extractive industries, there is no comprehensive international agreement;[53] hence the process restriction proposition suggests that the direction of the race is towards laxity.

Asset specificity

Companies with low asset specificity may move to less highly regulated countries in the face of costly regulation or inexpensive relocation. However, extractive industries are capital intensive with high sunk costs and are site specific[54]. Extractive industry assets are specific to the extent that they cannot easily be deployed elsewhere without losing considerable value. Therefore, it is less likely for companies to simply fly away and relocate production to a new location.

They may use other options: lobbying, educating, and litigating regulations that reflect their interests, or mutely accept whatever regulations come their way. Mutely accepting the regulations is, however, not a choice for MNCs in oligopolistic markets. This relates to the second proposition - industrial structure.

Industrial structure

The structure of the extractive industries of developing countries is oligopolistic with limited competition[55]. When the market is oligopolistic, corporations enjoy greater bargaining power over the state. Power of MNCs in developing countries is widely discussed in the academic literature.

They may lobby or 'educate' host government's ex-ante and ex-post regulatory changes and their transaction costs. They may even engage in activities to push their home government to exert pressure on the host government to change policies.

Transaction that requires a firm to make an asset specific investment makes the firm vulnerable because the value of the investment would be low if the intended transaction does not go through. To induce the firm to accept the risk of investing in the economy, the host government can offer a range of concession agreements such as tax holidays.

The obsolescing bargain theory however suggests that the bargaining power shifts to the host state in resource extraction industries after the investment is sunk.[56] The increased pressure from the public on the host state to raise demands on the investor and the ex post immobility of the MNC create a situation where the attractive agreement first carved out by the corporation will become obsolete. Theoretically, obsolescence can take the form of renegotiated contracts, higher taxes, expropriation of assets, or seizure of the income stream of the firm.

Thus investors are concerned that governments may exploit their initial position or try to alter the terms of the initial agreement. Powerful MNCs with highly vulnerable investments will naturally seek ways to protect their investment while trying to keep the production costs low.

If Murphy's arguments were suitable for developing countries that are dependent on extractive industries, MNCs would push for common regulatory outcomes

[53] *See* Maria Cecilia G Dalupan, *Mining and Sustainable Development: Insights from International Law, in*INTERNATIONAL AND COMPARATIVE MINERAL LAW AND POLICY, TRENDS AND PROSPECTS, 149, 153 (E.Bastida, T.Waelde, J. Warden-Fernandez, eds., 2005).

[54] *See* Otto &Cordes, *supra note*38.

[55] *Id.*

[56] *See generally* Raymond Vernon, *The Obsolescing Bargain: A Key Factor in Political Risk,in*THE INTERNATIONAL ESSAYS FOR BUSINESS DECISION MAKERS 281 (Mark B. Winchester ed., 1980).

across borders and stringent homogeneity internationally. He has argued that higher homogenous regulations act to harmonize contracts and firms with multinational asset specificity support these regulations[57]. However, the direction is not towards stringent homogeneity as Murphy claims. Instead, MNCs have opted to contract with host countries and there is still no comprehensive international agreement on mining.[58] For the support of the MNCs, the FDI source countries chose to protect their investment by bilateral investment agreements (BITs) (arguably because of lobbying of MNCs) which put host countries in disadvantage.[59]

4. Stimulation of the race to the bottom – contracting with host governments

The contractual rationale behind BITs and state contracts is to manage the obsolescing bargaining problem: the 'political risk' they face[60] and adverse changes to the law are the most feared legal risks of mining investors[61].

BITs: The main purpose of these treaties is to protect foreign investors in developing countries.[62] The clauses most relevant to the extractive industries in these treaties are those on international arbitration and the prohibition of expropriation without compensation.

It has been argued that international arbitration may disadvantage developing countries, due to the high cost of disputes[63], their lack of expertise and experience in dealing with arbitration and structural biases within the system.[64]

The second clause in BITs concerning the mineral industry is the prohibition of expropriation without compensation. It is indeed fair to include the prohibition of direct expropriation. However, one type of indirect expropriation - regulatory taking is becoming a particular point of concern from the perspective of public policy. Regulatory takings 'are those takings of property that fall within the police powers of a State, or otherwise arise from State measures like those pertaining to the regulation of the environment, health, morals, culture or economy of a host country'.[65]

There is no comprehensive definition of what constitutes a regulatory taking with many tribunals and academics suggesting that a determination as to the occurrence of an expropriation can only truly be undertaken on a case-by-case basis, in light of all attending circumstances.[66] If the definition is too expansive, it could impose potentially huge financial obligations on governments, make them fearful of potential litigation, create disincentives

[57] *See* Murphy, *supra note* 5, at 35.
[58] See generally Dalupan, supra note 53.
[59] See Tienhaara,supra note9, at 376.
[60] Political stability is one of the main concerns for foreign investors with high asset specificity. *See* Thomas W. Waelde& George N'di, *Stabilizing International Investment Commitments: International Law Versus Contract Interpretation*, 31 Tex. Int'l L.J. 216 (1996).
[61] *See* Robert Pritchard, *Safeguards for Foreign Investment in Mining,in*International and Comparative Mineral Law and Policy: Trends and Prospects, 73, 80 (E. Bastida, T. Walde, & J. Warden-Fernańdez, Eds., 2005).
[62] See generally Mary Hallward-Driemeier, Do Bilateral Investment Treaties Attract Foreign Direct Investment? Only a Bit...and They Could Bite, (World Bank Policy Research Working Paper, 2003), available at http://ssrn.com/abstract=636541 (last visited July, 04, 2012).
[63] Countries can expect an average tribunal cost US$400,000 or more in addition to the US$1-2 million in legal fees. *See* UNCTAD, *Investor-State Disputes and Policy Implications* 7 (2005), *available at* http://unctad.org/en/docs/c2d62_en.pdf (*last visited June, 14, 2012*).
[64] See generally Carlos G. Garcia, All the Other Dirty Little Secrets: Investment Treaties, Latin America, and the Necessary Evil of Investor-State Arbitration, 16 Fla. J. Int'l L 301 (2004); Luke, E. Peterson, All Roads Lead Out of Rome: Divergent Paths of Dispute Settlement in Bilateral Investment Treaties,inInternational Investment for Sustainable Development: Balancing Rights and Rewards 123 (L. Zarsky Ed., 2005).
[65] *See* UNCTAD, *Taking of Property* 12 (2000), *available at* http://unctad.org/en/docs/psiteiitd15.en.pdf (*last visited march, 25, 2012*).
[66] *See* L. Yves Fortier, Stephen L. Drymer, *Indirect Expropriation in the Law of International Investment: I Know It When I See It, or Caveat Investor,* 19(2) ICSID Rev/FILJ 293, 314 (2004).

to enact health and safety regulations, and introduce multiple distortions and social inefficiencies.[67] On the other hand, a definition that is too restrictive would obliterate a key investment guarantee that protects foreign investors.[68]

Huge financial obligations that could be imposed on governments relate to not only the legal costs associated with defending a regulation in international arbitration, which can be significant, but also to the potential compensation payments that can be awarded to the investor if a tribunal determines that an expropriation has occurred.[69]

State contracts: In addition to any general commitments to investment protection made by a state under international agreements with other states, there may also be specific protections offered to mineral investors through contracts made directly with investors. In most developed countries mining rights are based only on law and regulation, however developing countries have relied far more on agreements with investors referred to as 'state contracts' or 'concession agreements'.[70]

State contracts contain investor protections which are not generally found in international agreements. Since the resource extraction sector has particularly high asset specificity, and investments have a greater need for stability than other shorter-termed industrial projects[71], one method of managing the risk of adverse change in law is the use, in national law or state contracts, of stabilization clauses, which seek to preserve the law of the host country as it applies to the investment at the time the state contract is concluded, and which ensures that the future changes to the law of the host country are inapplicable to the foreign investment contract.[72]

Quite extensive stabilization clauses have emerged[73] and include not only the stability of the fiscal regime, but also the imposition of new obligations by subsequent regulation or by an administrative/judicial ruling re-interpreting existing law. Such clauses may be problematic from the perspective of the regulator in terms of environmental management.

This is a dynamic activity, responding to growing knowledge concerning the environment and anthropogenic threats to it, as well as to changing perceptions concerning the seriousness of these threats. An added level of complexity derives from the continuous development of technologies designed to protect the environment. As these technologies become available, policy must adjust to reflect new capabilities.[74]

Applying the constraints of stability to the regulation, particularly in the developing world, is thus a subject of legitimate concern. Some authors have questioned the binding character of stabilization clauses, arguing that states cannot waive their sovereignty in such a manner.[75] However, despite the academic

[67] *See* Kevin, R. Gray, *Foreign Direct Investment and Environmental Impacts – Is the Debate Over?*, 11(3) RECIEL 306, 311 (2002).

68 See generally Julie A. Soloway, Environmental Expropriation under NAFTA Chapter 11: The Phantom Menace, in LINKING TRADE, ENVIRONMENT, AND SOCIAL COHESION: NAFTA EXPERIENCES, GLOBAL CHALLENGES 131 (J. Kirton& V.W. MacLaren, Eds., 2002).

[69] *See* Tienhaara, *supra note* 9, at 379 (*citation omitted*).

[70] *See* UNCTAD, *Management of Commodity Resources in the Context of Sustainable Development: Governance Issues for the Mineral Sector* 9 (1997), *available at* http://archive.unctad.org/en/docs/poitcdcomd3.en.pdf*(last visited June, 20, 2012)*; UNCTAD, *State Contracts: Issues in International Investment Agreements* 3 (2004), *available at* http://archive.unctad.org/en/docs/iteiit200411_en.pdf*(last visited June, 20, 2012)*.

[71] Piero Bernardini, *Investment Protection under Bilateral Investment Treaties and Investment Contracts*, 2 (2) J. WORLD INV. 235, 236 (2001).

[72] *See* UNCTAD (2004), *supra note* 70, at 26.

[73] *See generally* Waelde & N'Di, *supra note* 60.

[74] K. von Moltke, *International Investment and Sustainability: Options for Regime Formation,in*THE EARTHSCAN READER ON INTERNATIONAL TRADE AND SUSTAINABLE DEVELOPMENT 347, 358 (K. Gallagher & J. Werksman, Eds., 2002).

[75] *See* Bernardini, *supra note* 71, at 242; M. SORNARAJAH, THE INTERNATIONAL LAW ON FOREIGN INVESTMENT 408 (2nd ed., 2004).

debate, the crucial point is that tribunals have frequently affirmed the validity of such clauses.[76]

In some cases, stability clauses also prevent countries from living up to their other international obligations. Amnesty International's description of the stability agreements that Chad and Cameroon entered into with a consortium of oil companies illustrates this point. Amnesty International argues that the agreements could allow those countries to ignore their human rights obligations by claiming that they prevent them from taking measures that would de-stabilize the financial equilibrium.[77]

Another problem with multiple investor-state agreements is that they prevent host states from developing consistent and coherent investment policies. By entering into agreements that supersede domestic legislation, host states risk creating policy incoherence.[78] This approach can have a negative impact because it decreases the incentive to develop local institutions. Tom Ginsberg argues that in this way international investment agreements can decrease the quality of governance in host states.[79]

When governments are bound by stability agreements and the risk of international arbitration disputes, investors have the option to challenge new, more restrictive measures in international arbitration. An investor should expect some level of environmental regulation and management in response to either heightened environmental awareness or the discovery of new ecological problems, which must be internalized as a risk of investment.[80] Having an option to challenge a new measure allows the investor to reallocate the risk to the regulator, and perhaps avoid the polluter pays principle so that the general taxpayer bears the burden.[81]

5. Evidence from developing countries

The above mentioned propositions of concentrated industrial structure, high asset specificity, the importance of process restrictions and little or no market access restrictions hypothetically suggest that the direction of the race is towards the bottom in developing countries with a dependency on extractive industries. Some scholars seem to agree that a race to bottom may exist in certain sectors, namely in the natural resources sector.[82] We do, however, need evidence of this. In the extractive industry, the most relevant fields are taxation and environmental law.

a. Taxation law

Tax exemption policy is one of the exploitative policies that are similar to regulatory laxity or non-tariff subsidies in terms of attracting foreign direct investment.[83] One study was conducted on a dataset of corporate income tax regimes in 50 emerging and developing economies over the period 1996-2007 which analyzed their impact on corporate tax revenues. It argues that there is a partial race to the bottom: while countries with standard tax

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[76] GaetanVerhoosel, *Foreign Direct Investment and Legal Constraints on Domestic Environmental Policies: Striking a "Reasonable" Balance Between Stability and Change*, 29(4) Law &Pol'y Int'l Bus 451, 456 (1998).

[77] Amnesty International, *Contracting out of Human Rights: The Chad-Cameroon Pipeline Project* (2005), *available at* http://www.amnesty.org/en/library/info/POL34/012/2005 (*last visited February, 14, 2012*)

[78] UNCTAD, *Reserving Flexibility in IIAs: The use of Reservations* 5 (2006).

[79] See generally Tom Ginsberg, International Substitutes for Domestic Institutions: Bilateral Investment Treaties and Governance, 25 INT'L REV. OF L. & ECON. 107 (2005).

[80] Waelde and Ndi note that the impositions of new regulations or judicial decisions are indeed relevant consideration for investors. *See* Waelde & Ndi, *supra note* 60, at 230.

[81] *See*Verhoosel, *supra note* 76, at 456.

[82] See generally, Gray, supra note 67.

[83] Cooper identified different policy outcomes of interdependence: constructive, passive, defensive, aggressive and exploitative. He mentioned flags of convenience, lax disclosure requirements, foreign subsidies and tax havens as examples of exploitative policies. *See generally* Richard N. Cooper, *Economic Interdependence and Foreign Policy in the Seventies*, 24(2) World Polit 160 (1972).

regimes have developed corporate tax systems in a similar fashion as advanced economies, countries that have been under pressure to lower tax rates in order to lure and boost investment are sinking to the bottom, most notably in the case of Africa, creating effectively a parallel tax system. It also states that developing countries have made widespread use of tax incentives granted under special regimes, which has brought effective tax rates close to zero in many countries.[84]

This study computes effective tax rates to take account of complicated special regimes, such as partial tax holidays, temporarily reduced rates and increased investment allowances. We have to note that this study is not focused on any particular industry. However, this study offers an important conclusion: when a special tax regime is used to attract foreign direct investment, the race is towards the bottom.

There are a few studies that have been solely conducted in the mining industry of developing countries. For example, one study conducted in Ghana examined tax incentive regimes and tax concessions provided by the fiscal regime of the mining laws and negotiated investment agreements and stated that 'government revenue generation is constrained by the range of capital allowances, list of mining-related equipment and items exempted from customs and import duties, the nonpayment of capital gain taxes, dividend withholding taxes, corporate income taxes, the huge offshore sales revenue retentions and the payment of royalty at the lowest allowable rate.'[85] UNCTAD also confirmed in its 2006 report that Ghana took particular measures aimed at lowering corporate income taxes. In 2010, Ghana became a major host country for FDI in the oil industry.[86] Egypt also took measures to lower taxes and Egypt was the leading recipient of FDI in Africa in the projects of non-oil extractive industries.[87] In Mali, mining law reform in 1999 led to led to a reduction in benefits to the state and increased advantages conceded to the mining companies. These advantages involve less government participation in the capital of companies, lower taxes and accelerated depreciation.[88]In Kyrgyzstan, the government gave tax advantages to foreign investors that they withheld from local businesses driving many local ventures out of business. This created a political counter-current and the government reacted by removing the tax advantages which in turn drove away a majority of the foreign investors.[89] As noted by Barberis, there is a trend towards the overall reduction of taxation levels in mining globally.[90]

b. Environmental law

There is an increasing view that weak environmental protection regimes are a form of subsidy to polluting producers.[91] The failure to maintain environmental protection at an appropriately high level provides illicit subsidies to the business. By absorbing the environmental costs

[84] *See generally* Ali S. M. Abbas, Alexander Klemm, Sukhmani Bedi & Junhyung A. Park, *Partial Race to the Bottom: Corporate Tax Developments in Emerging and Developing Economies* (IMF working paper, 2012), *available at* http://www.imf.org/external/pubs/ft/wp/2012/wp1228.pdf(*last visited February, 10, 2012*).

[85] T. Akabzaa, *Mining in Ghana: Implications for National Economic Development and Poverty Reduction*, *in* Mining in Africa: Regulation and Development 25, 26 (B. Campbell, ed., 2009).

[86] SeeUNCTAD, World Investment Reportxiii (2011), available at http://www.unctad-docs.org/files/UNCTAD-WIR2011-Full-en.pdf(last visited June, 29, 2012).

[87] See UNCTAD,supra note 36, at 114.

[88] *Seegenerally* Gisele Belem, *Mining, Poverty Reduction, the Protection of the Environment and the Role of the World Bank Group in Mali*, in Mining in Africa: Regulation and Development 119 (B. Campbell, ed., 2009).

[89] William F. Arnold, *Mongolian Mining Sector Competitiveness and the Use of Stability Agreements* IV-4 (Economic Policy Reform and Competitiveness Project, US Agency for International Development, 2004), *available at* http://pdf.usaid.gov/pdf_docs/Pnadb651.pdf*(last visited June, 20, 2012)*.

[90] *See* Daniele Barberis, Negotiating Mining Agreements: Past, Present and Future Trends 160 (1998).

[91] *See*Trachtman, *supra note* 4, at 56 (*citation omitted*).

of production, in a context where the environmental costs of production might otherwise be charged to the producer, a country can assist its producers by lowering their costs of competing in either foreign or domestic markets.

In Zimbabwe, a country whose mining sector is dominated by foreign enterprises, the Mines and the Minerals Act supersedes all other legislation including statutes governing the protection of the environment.[92] The Moroccan and Tunisian governments have shown reluctance to upgrade the level of regulation of the phosphate industry in response to the possibility that these companies may flee to countries having less environmentally regulatory scope.[93] The government of Ghana granted mining licenses in forest reserve areas in the belief that it risked losing investment and being forced to compensate the involved companies.[94] In Zambia, foreign investors are exempt from environmental liabilities for past activities and can defer compliance with environmental standards.[95] Even in the extractive industries of developed countries, similar outcomes are evident: before the introduction of federal laws, US states with powerful coal industries tended to ignore the environmental consequences of coal mining.[96]

Also there is a view that special economic zones are racing to the bottom[97] since these zones are developed solely for foreign investors to take advantage of special legal regimes geared towards export oriented production and governments use various instruments to attract investment and those are not generally applicable to other parts of a country.[98] However there are similarities between special economic zones and extractive industries in developing countries. Extractive industries in most developing countries are export oriented (excluding Russia, Brazil and China, since they have huge domestic appetite for primary commodities) and as we have discussed before, in order to attract FDI, host governments use different policy tools than they do with domestic investment in extractive industries.

Some scholars argue that environmental costs make up only a small proportion of a company's total costs; they will have a little impact on firm's location decisions.[99] There is little evidence that MNCs select their investment sites based on low environmental standards. Indeed investors usually do not include environmental regulation as a substantial factor when deciding on the location of their investment.

However a race to the bottom is not restricted to investor's decision on where to locate. It is acknowledged that established companies may apply pressure to host governments to lower, not raise, or not enforce environmental regulations.[100]

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[92] *See* Gray, *supra note* 67, at 309.

[93] *See*Vogel, *supra note* 24, at 34.

[94] *See* Tienhaara, *supra note* 9, at 389. Tienhaara conducted a confidential interview with a forestry official of Ghana who said restoring the forest is a myth: 'You fell tropical trees and in place you plant grass and ornament trees- you fell mahogany and plant cassia, it is not the same… After mining the soil is unable to sustain indigenous species'.

[95] *See* OECD, *Foreign Direct Investment and the Environment: Lessons from the Mining Sector* 10 (2002), *available at* http://www.oecd.org/investment/investmentpolicy/44320363.pdf*(last visited July, 01, 2012)*.

[96] *See generally* Jonathan Rodden & Susan Rose-Ackerman, *Does Federalism Preserve Markets?*, 83 Va.L.Rev.1534 (1997). *See also* Kirsten Engel & Susan Rose-Ackerman, *Environmental Federalism in the United States: The Risks of Devolution,in* Regulatory Competition and Economic Integration: Comparative Perspectives 135 (D. C. Esty & D.Geradin, eds., 2001).

[97] *See* Gray, *supra note* 67, at 309.

[98] *See generally* W. Ge, *The Dynamics of Export Processing Zones* (UNCTAD discussion paper, 1999), *available at* http://archive.unctad.org/en/docs/dp_144.en.pdf*(last visited May, 10, 2012)*.

[99] *See generally* CHARLES P. OMAN, POLICY COMPETITION FOR FOREIGN DIRECT INVESTMENT: A STUDY OF COMPETITION AMONG GOVERNMENTS TO ATTRACT FDI (2000).

[100] *See* Zarsky,*supra note* 45, at 395. Zarsky notes that MNCs do not actively seek out a 'pollution haven' but—if local environmental regulation is weak—create one through their operations. *See also* N. Mabey& R. McNally, *Foreign Direct Investment and the*

OECD reported that the avoidable impacts of extractive industries, such as biodiversity loss, waste disposal and discharge have occurred in many developing countries due to regulatory failures in the environmental field. Weak governance and in particular in the areas of environmental regulations and their administering institutions has enabled substandard mining to occur.

Even when governments adopt more stringent rules, they may lack motivation to enforce these rules. These rules are either too costly for their capacity or other factors, such as the rent seeking behavior of government (or government officials and political figures) or lobbying of interest groups may effectively hinder their implementation. For example, after the breakdown of the former Soviet Union and the transition to a more democratic political system, and the emergence of market economies in Central and Eastern Europe, nearly all governments in the region adopted more stringent environmental regulations based on US and Western Europe standards. However, few governments in the region have adequate financial resources to clean up the environmental damage that has occurred or to enforce these new environmental regulations effectively.[101]

Sub-Saharan African countries are currently enacting, or have recently enacted, environmental protection legislation. In some cases, however, regulations defining the application of the law have yet to be drafted or promulgated. The delays may be several years, inhibiting enforcement efforts. For example, in Cameroon environmental legislation was enacted in 1996 but the implementing regulations have yet to be drafted.[102]

Regulatory competition has taken a toll on those countries which failed to include the costs to the businesses that should be internalized. Externalization not only occurs on a broad base in the territory of the state that maintains weak environmental regulation. The environmental degradation may have effects on specific groups which is mostly the case with the effects of extractive industries. In this selective externalization, the polluting industry is able to externalize the costs to the affected groups and costs are borne by the local community. Because of the fact that externalization is often selective in extractive industries and tax revenues are often not channeled to communities in the regions where investment takes place, a cost and benefit analysis undertaken at the national level is unlikely to show such inequalities at the local level and fail to internalize costs related to pollution.

Extractive industries remain inherently problematic from an environmental point of view, even though there seems to be a good understanding of its direct environmental impacts. It is a well-established fact that host governments for do not always establish appropriate environmental regulations or assure their robust enforcement.

6. Conclusion

As discussed above, the structure of regulatory competition implies a race to the bottom in developing countries with a dependency on extractive industries. This paper has argued that competition among developing countries dependent on extractive industries is leading to a race to the bottom. Competition among host governments to attract investment may lead to a lax regulatory environment, a reluctance to enforce existing laws and regulations, and self-strangling agreements with MNCs and FDI home countries.

Environment:From Pollution Haven to Sustainable Development (WWF, 1999), *available at*http://www.oecd.org/dataoecd/9/48/2089912.pdf*(last visited June, 11, 2012).*

[101] *See generally* Denis A. Rondinelli&GyulaVastag, *Private Investment and Environmental Protection in Central and Eastern Europe: ALCOA-Kofem's strategy in Hungary*, 16(4) EMJ 422 (1998).

[102] *See* OECD,*supra note*95, at 41.

The propositions of product restriction and industrial structure support this conclusion. The asset specificity proposition, however, offered different implications than those which are conventionally suggested and also seems to support the 'race to bottom' notion in developing countries with a dependency on extractive industries.

Exclusive factors attributable to mining industry dependent developing countries such as the overall low level of governance of host countries, the nature of the commodity, industrial structure, the priority area of FDI, the government's dependence on extractive industry revenue, the impact on the environment and society support the theoretical implication. Increasing competition amongst developing countries with a dependency on extractive industries has led to a relaxation of regulations, the circumvention of existing legal frameworks, potential future changes in the legal framework protecting investors through bilateral investment treaties and state contracts that inevitably limit the adjusting capability of domestic policy and arguably the relaxation of enforcement of the existing laws and regulations.

However, it's important to note that every country has its own unique conditions which inevitably affect its investment environment. Mongolia, the situation is not necessarily a 'race to bottom', rather there are fluctuating changes in the legal framework of mining. Case study on Mongolia shall be deemed important, though this paper does not include part of my research on Mongolia. Indeed, it's an open subject for researchers for the future exploration.

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AD HOC ARBITRATION IN MONGOLIA: A PROCEDURAL OVERVIEW

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Preamble

In recent times, disputes arising from private relations have greatly increased and have become more complex as each country's market economy becomes more closely intertwined with other foreign countries due to globalization. Methods of dispute resolution have also evolved. No longer is dispute resolution limitedonly to litigation, but haschanged and developedto be more suitable and flexible for parties in handling complex disputes. Arbitration is one suchform of alternative dispute resolution which occurs outside the traditional court system, and which has become increasingly widespread in the practice of law.

Introduction

Compared to litigation, the parties to arbitral proceedings play more active roles in choosingthe rules, forum, and procedures of dispute resolution. For example, parties choose procedural rules and may also select arbitrators and the number of them. Parties may also choose the location of arbitration, the language of arbitral proceedings, and more. However, there are certain aspects of arbitration that are less desirable than those found in a traditional court system. In most arbitration proceedings, parties do not have theright to appeal a final award even if the parties believe the arbitral tribunal was mistaken in its decision. Nevertheless, in terms of efficiency and flexibility in dispute resolution, arbitration has advantages over litigation. As such, it is important to understand the role of arbitration in Mongolia's judicial system. In particular, we consider the role of ad hoc arbitration in an effort to provide readers with an overview of existing procedures which govern the process in Mongolia.

Differences between Institutional and Ad Hoc Arbitration in Mongolia

The *Arbitration Law*, Article 5.1 states that, in Mongolia, "arbitration shall be either institutional or ad hoc."[1] Article 4.1.1 defines institutional arbitration as "arbitration, set up for the purpose of conducting arbitral proceedings permanently."[2] Ad hoc arbitration is defined by Article 4.1.2 as "arbitration, set up for settling a particular dispute, at one time, between the parties."[3] With regard to institutional arbitration, Article 5.2 states that institutions such as the Mongolia International and National Arbitration Center ("MINAC") or other non-governmental organizations and their associations, may undertake institutional arbitration.[4] Once parties engage such institutions to handle institutional arbitration, the procedures for arbitration

[1] Arbitration Law, art. 5.1 (2003) (Mong.).
[2] *Id.* at art. 4.1.1.
[3] *Id.* at art. 4.1.2.
[4] *Id.* at art. 5.2.

and the list of arbitrators that may be utilized are regulated by the stipulated rules and procedures (e.g., the Charter) of the chosen institution, pursuant to the *Arbitration Law*,Articles 5.4 and 5.5.[5]

On the other hand, the *Arbitration Law*, Article 5.7 provides thatad hoc arbitration may be set up and procedural rules chosen by the parties via written agreement.[6] For example, the parties may choose their own arbitrators without restriction, except for those that are prohibited by law. Moreover, Article 5.8 states that the parties to ad hoc arbitration shall have the same rights as parties to institutional arbitration.[7] These rights, as stated above, include choosing arbitrators and appointing authorities, designating the location and language of arbitration, and so forth. Parties are free to choose the place of arbitration either in institutional or ad hoc proceedings pursuant to the *Arbitration Law*, Article 24.[8] Thus, ad hoc arbitration, while guaranteeing the same rights as institutional arbitration, presents a more flexible alternative to parties who wish to manage the process of arbitration.

Relationship between UNCITRALRules and Mongolian Arbitration Rules in Ad Hoc Proceedings

In accordance with the *Arbitration Law*, Article 5.7, the parties set up ad hoc arbitration via a written agreement.[9]The *Arbitration Law*,Articles23.1 and 24 specifically state that the parties are free to agree upon the place of arbitration and the procedural rules to be followed by an arbitral tribunal when conducting arbitration.[10] Although the *Arbitration Law*,Article 3.1 states that the law will be applied within the territory of Mongolia, whenever arbitration is proposed to settle a dispute, parties in Mongolia are free to choose *UNCITRAL Rules*, Mongolian *Arbitration Law*, or any other arbitration rules they deem fit, such as *ICC Rules*, and also to choose the location to settle thedispute.[11] In other words, there is no restriction on choosing foreign or international arbitration rules underMongolian law, unless the parties agree to chooseMongolia's *Arbitration Law*. If, for example, the parties choose Korean arbitration law to govern arbitral proceedings in Mongolia, the Korean law shall govern the procedural process over such a dispute. Conversely,if the parties in Mongolia choose *UNCITRAL Rules* and the Korean Commercial Arbitration Boardas the locus, the ad hoc arbitration will be held in Korea and will be governed by *UNCITRAL Rules*. If parties agree on *UNCITRAL Rules* and the place of ad hoc arbitration to beMongolia, the proceedings shall be governed by *UNCITRAL Rules* while the ad hoc arbitration will occur in Mongolia. In the latter case, parties may still request assistance from MINAC, if the parties so choose.

Ad Hoc Arbitration Procedures in Mongolia

Drafting Contractual Provisions

As stated, the *Arbitration Law*, Article 5.7 provides that parties may set up ad hoc arbitration through written agreement. In other words, parties may decide upon procedural process and rules of arbitration when drafting arbitration provisions under contract.[12] For example, parties may agree to choose (1) either the *Arbitration Law*,*UNCITRAL Rules*, or other preferred rules, (2) the appointing authority, (3) the number of arbitrators, (4) the location of arbitration, and (5) the language to be used in arbitral proceedings.

A sample ad hoc arbitration clause may appear as follows:

"This Agreement shall be subject to the laws of Mongolia and shall be deemed to be made in Ulaanbaatar, Mongolia. Any

[5] *Id.*at arts. 5.4, 5.5.
[6] *Id.*at art. 5.7.
[7] *Id.*at art. 5.8.
[8] *Id.* at art. 24.
[9] *Id.*at art. 5.7.
[10] *Id.*at arts. 23.1, 24.
[11] *Id.*at art. 3.1.
[12] *Id.*at art. 5.7.

dispute, controversy, or claim arising out of or relating to this Agreement, or breach, termination or invalidity thereof, shall be resolved by ad hoc arbitration, before a single arbitrator, pursuant to UNCITRAL arbitration rules at the office of Anderson & Anderson LLP in Mongolia. The language of arbitration shall be English."

Selecting Arbitrators and Appointing Authorities

According to the *Arbitration Law*, Articles 14.1, 14.2, and 14.3, parties are free to compose an arbitral tribunal consisting of a sole arbitrator or panel of arbitrators.[13] If the parties fail to make this determination in contract, the number of arbitrators shall, by default, be three. This is consistent with the *UNCITRAL Rules*, Article 7.1, which more specifically provide the parties thirty days within which to determine the makeup of an arbitral panel.[14] In the case of three arbitrators, the *UNCITRAL Rules*, Article 9 and the *Arbitration Law*, Article 15.3 state that each party shall appoint one arbitrator and the two arbitrators shall thereafter appoint a third arbitrator as the presiding arbitrator.[15]

With regard to the choice of arbitrators, there is a distinction between *UNCITRAL Rules*and the *Arbitration Law* requirements. While *UNCITRAL Rules* do not state any qualifications for potential arbitrators, the *Arbitration Law*, Articles 15.1 and 15.2 impose restrictions that potential arbitrators may not be members of the Mongolian Constitutional Court, a judge, a prosecutor, a case registrar, a detective, an officer of court enforcement, an advocate or notary who had previously worked with/for any of the parties, or other officials who are prohibited to conduct work which isnot related to their legal duties.[16] With the exception of the aforementioned persons, the parties to arbitration are free to choose any local persons as arbitrators in Mongolia. However, if a foreign party selects a local Mongolian individual as an arbitrator, there can be some impediments. Particularly, there are few arbitrators in Mongolia who have experience in dealing with international arbitration and are able to speak English fluently. This can be disadvantageous to parties who choose to conduct arbitral proceedings in English as they may require the services of a professional English translator.

In addition to those described above, there is another distinction between the *UNCITRAL Rules* and *Arbitration Law*. This distinction occurs when one party fails to choose the second arbitrator within thirty days after such party receives the other party's request to appoint an arbitrator, or when two appointed arbitrators fail to agree on the third arbitrator within thirty days of their appointments. According to the *UNCITRAL Rules*, Article 9, the parties or arbitrators may request the appointing authority to select the second arbitrator or the presiding arbitrator.[17] Should the parties or arbitrators fail to do so, the *UNCITRAL Rules*,Article 6 state that any institution or person, including the Secretary-General of the Permanent Court of Arbitration at Hague, can be designated as the appointing authority, unless the parties have already agreed upon the choice of the appointing authority.[18] On the other hand, the *Arbitration Law*, Article 15.5 specifically states that upon the parties' request,selection of the appointing authority shall be made by the Mongolian Court of Appeals.[19]In the case of a sole arbitrator and according to *UNCITRAL Rules*, Article 8.1, the parties should agree upon the appointment of the sole arbitrator, with the designated appointing authority providing this service in the event the parties are unable to

[13] *Id.*at arts. 14.1, 14.2, 14.3.

[14] UNCITRAL, United Nations Commission on International Trade Law, art 7.1, G.A. Res. 65/22, U.N. Doc. A/RES/65/22 (revised 2010) [hereinafter UNCITRAL].

[15] *Id.* at art. 9; *Arbitration Law*, art. 15.3 (2003) (Mong.).

[16] Arbitration Law, arts. 15.1, 15.2 (2003) (Mong.).

[17] UNCITRAL, *supra* note 14 at art. 9.

[18] *Id.* at art. 6.

[19] Arbitration Law, art 15.5 (2003) (Mong.).

agree.[20] However, the *Arbitration Law*, Article 15.6 stipulates that if the parties are unable to reach an agreement regarding the appointment of an arbitrator, the sole arbitrator shall be appointed by the Court of Appeals based on the requests of the interested parties.[21]

As the differences between the *Arbitration Law* and *UNCITRAL Rules* have demonstratedabove, the *UNCITRAL Rules* are arguably more advantageous and more flexible and manageable for parties than the *Arbitration Law*. For example, if the parties select *UNCITRAL Rules* to guide arbitral proceedings, the parties may choose a Mongolian judge or any other person as an arbitrator. This process is more restrictive under Mongolia's *Arbitration Law*. Moreover, with regard to the choice of appointing authorities, the *UNCITRAL Rules* are far more flexible in that they impose no restrictions on the selection of appointing authorities. Under the *Arbitration Law*, on the other hand, the Court of Appeals must play a role as the appointing authority upon the parties' request and will appoint arbitrators if the parties fail to agree on such appointments. Therefore, in terms of flexibility and independent decision-making, the *UNCITRAL Rules* are more preferable for parties to ad hoc arbitration.

The Exchange of Evidence

In regard to the exchange of evidence, the *Arbitration Law*, Article 27.5 states that parties may submit all relevant documents, including references to the documents and evidence, with their statements.[22] In addition, pursuant to the *Arbitration Law*,Article 28.4, all statements, documents, or other information supplied to the arbitral tribunal by one party shall be communicated to the other party;any expert reports or evidentiary documents that may be used in proceedings by the arbitral tribunal shall also be communicated to the parties.[23] If any party fails to produce documentary evidence, the arbitral tribunal may continue with the proceedings and make a decision and award based on the evidence that was presented before it in accordance with the *Arbitration Law*, Article 29.1.3.[24]

Alternatively, the *UNCITRAL Rules* do not impose upon parties the requirement to communicate to the other party with regard to the exchange ofevidence.The *UNCITRAL Rules* instead require each party to bear the burden of proving the facts relied on to support its claim or defense pursuant to Article 27.1.[25]Compared to the *UNCITRAL Rules*, the *Arbitration Law* provides better opportunities for parties to prepare for arbitration proceedings in that they are required to communicate all evidence to eachother. This assistsa partyto understandwhat the other party is going to argue inarbitration and provides the parties with the opportunity to better prepare argumentsprior to a hearing.

The Request for Production of Evidence and Interim Measures

As stated, if any party fails to produce documentary evidence, the arbitral tribunal may continue with proceedings and make a decision and award based on the evidence that was presented before it, pursuant to the *Arbitration Law*,Article 29.1.3.[26]Additionally, in accordance with the *Arbitration Law*, Article 33, the arbitral tribunal or a party with the approval of the arbitral tribunal, may request assistance in gathering evidence from the Mongolian Court of Appeals.[27] The Court of Appealsmay execute such a request in compliance with the *Code of Civil Procedure*,Article 46.[28]Furthermore, pursuant to the *Arbitration Law*, Article 21, the arbitral tribunal may order any party to take interim measures of protection, if necessary,andalsomayrequireanypartyto

[20] UNCITRAL, *supra* note 14 at art. 8.1.
[21] *Id.* at art. 15.6.
[22] Arbitration Law, art 27.5 (2003) (Mong.).
[23] *Id.* at art. 28.4.
[24] *Id.* at art. 29.1.3.
[25] UNCITRAL, *supra* note 14 at art. 27.1.
[26] Arbitration Law, art. 29.1.3 (2003) (Mong.).
[27] *Id.* at art. 33.
[28] *Id.*

provide appropriate security in connection with such measures.[29]According to the *Arbitration Law*, Article 13.1,a party may request the Court of Appeals to order interim measures of protection before or during arbitration proceedingsand ajudge may undertake such interimmeasures as per the *Code of Civil Procedure*, Article 69.[30]

Similarly, *UNCITRAL Rules*, Article 27.3, state that "the arbitral tribunal may require the parties to produce documents, exhibits or other evidence at any time during the arbitral proceedings within such a period of time as the arbitral tribunal shall determine."[31] However, the *UNCITRAL Rules* do not provideany avenues through which a party may obtain evidence by asking for assistance from a court of law. In regard to interim measures related toevidence, the *UNCITRAL Rules*, Articles 26.1 and 26.2(d) clearly state that anarbitral tribunal may grant interim measures in order to "[p]reserve evidence that may be relevant and material to the resolution of the dispute."[32]*UNCITRAL Rules*,Article 26.6 further states that the arbitral tribunal may also"require the party requesting an interim measure to provide appropriate security in connection with the measure."[33] In addition, "a request for interim measures addressed by any party to a judicial authority shall not be deemed incompatible with the agreement to arbitrate, or as a waiver of that agreement"under *UNCITRAL Rules*,Article 26.9.[34]

Hearings

With regard to hearings, the *Arbitration Law*,Article 28.1 states that subject to any contrary agreement by the parties, the arbitral tribunal shall decide whether it will hold an oral hearing for the presentation of evidence or for oral arguments, or whether the procedures shall be undertaken based on documents and other materials, without an oral component.[35] In addition, according to the *Arbitration Law*, Article 28.2, the arbitral tribunal shall hold a hearing if requested by one of the parties unless the parties have agreed that no hearings shall be held.[36] In regard to the notice of hearings, the parties must be provided sufficient advanced notice of any hearings and of any meetings of the arbitral tribunal, especially when the arbitral tribunal carries out inspections on goods, property, or documents pursuant to the *Arbitration Law*,Article 28.3.[37]

According to *UNCITRAL Rules*,Article 28.1, in the event of an oral hearing,"the arbitral tribunal shall give the parties adequate advanced notice of the date, time and place" of any proceedings.[38]Unlike the *Arbitration Law*, *UNCITRAL Rules*, Article 28.3 requires that "[h]earings shall be held in camera unless the parties agree otherwise."[39]The *UNCITRAL Rules*also provide articles relating tothe closure and re-openingofhearings. Pursuant to Article 31.1,"[t]he arbitral tribunal may inquire of the parties if they have any further proof to offer or witnesses to be heard or submissions to make and, if there are none, it may declare the hearings closed."[40]According to Article 31.2, "[t]he arbitral tribunal may, if it considers it necessary owing to exceptional circumstances, decide, on its own initiative or upon application of a party, to reopen the hearings at any time before the award is made."[41]

Briefings

If the parties to arbitration agree to utilize the *Arbitration Law*, the parties'arbitration briefs must comply with the provisions set forth in Article 27 of the law. According to the *Arbitration*

[29] *Id.* at art. 21.
[30] *Id.* at art. 13.1.
[31] UNCITRAL, *supra* note 14 at art27.3.
[32] *Id.* at arts. 26.1, 26.2.
[33] *Id.* at art. 26.6.
[34] *Id.* at art. 26.9.
[35] Arbitration Law, art. 28.1 (2003) (Mong.).
[36] *Id.* at art. 28.2.
[37] *Id.* at art. 28.3.
[38] UNCITRAL, *supra* note 14 at art. 28.1.
[39] *Id.* at art. 28.3.
[40] *Id.* at art. 31.1.
[41] *Id.* at art. 31.2.

*Law,*Articles 27.1 and 27.2, a statement of claim must be in writing and signed by the claimant or its representative.[42] The requirements for the statement of claim are the same as those stipulated in the *Code of Civil Procedure*,Article 62, unless the parties have agreed otherwise.[43] In a statement of claim, the claimant must state the facts supporting claim, the points at issue, and the relief or remedy sought, while the respondent should state his or her defense(s) to the claims raised in accordance with the *Arbitration Law,*Article 27.5.[44] In regard to the respondent's rights, the respondent may choose to agree and perform the claim requirements to settle the case, or the respondent may deny the claims and submit a counterclaim, pursuant to the *Arbitration Law*, Articles 27.3 and 27.4.[45] Finally, the *Arbitration Law*,Article 27.6 states that either party is able to amend or supplement its claim or defense during the course of arbitral proceeding, unless the arbitral tribunal disagrees in order to prevent the delays that may be involved with making such amendments.[46]

Under the*UNCITRAL Rules*, Article 20.1, the claimant is responsible to "communicate its statement of claim in writing to the respondent and to each of the arbitrators within a period of time to be determined by the arbitral tribunal."[47]In accordance with Article 20.2(a)-(e), the statement of claim should include the following: the names and contact details of the parties; a statement of the facts supporting the claim; the points at issue; the relief or remedy sought; and the legal grounds or arguments supporting the claim.[48]The *UNCITRAL Rules* have similar requirements for the respondent under Article 21.1: "[t]he respondent shall communicate its statement of defense in writing to the claimant and to each of the arbitrators within a period of time to be determined by the arbitral tribunal."[49]Additionally, pursuant to Article 21.3, "[i]n its statement of defense, or at a later stage in the arbitral proceedings if the arbitral tribunal decides that the delay was justified under the circumstances, the respondent may makea counterclaim or rely on a claim for the purpose of a set-off provided that the arbitral tribunal has jurisdiction over it."[50]

Enforcement

In order to enforce an arbitral award in foreign countries, it does not matter whether a party chooses to use the *Arbitration Law* or *UNCITRAL Rules*. Rather, it is a matter of whether an enforcing country is a signatory of the *New York Convention*.[51]The *UNCITRAL Rules* do not include provisions regarding the enforcement of arbitral awards; however, the United Nations, in an effort to promote the use of international arbitration in commercial-related dispute resolution,established the *Convention on the Recognition and Enforcement of Foreign Arbitral Awards* (also referred to as the *New York Convention*)in 1958.[52]Since its entry into force in 1959, most United Nations member states have adopted the *New York Convention,*and are bound by its provisions.

Mongolia is one suchsignatory to the *New York Convention*. This means that one hundred fifty-one countries shouldrecognize and enforce Mongolian arbitral awards, with exceptions. In addition, arbitration decisions rendered in Mongolia maybe sent to aforeign authority designated for arbitration enforcement, so long as that state is also a member of the *New York Convention* and therefore bound to recognize Mongolian arbitral

[42] Arbitration Law, arts. 27.1, 27.2 (2003) (Mong.).
[43] *Id.* at art. 27.2.
[44] *Id.* at art. 27.5.
[45] *Id.* at arts. 27.3, 27.4.
[46] *Id.* at art. 27.6.
[47] UNCITRAL, *supra* note 14 at art. 20.1.
[48] *Id.* at art. 20.2.
[49] *Id.* at art. 21.1.
[50] *Id.* at art. 21.3.
[51] New York Convention, the Convention on the Recognition and Enforcement of Foreign Arbitral Awards, 330 UNTS 38, 21 UST 2517, 7 ILM 1046 (1958) [hereinafter New York Convention].
[52] *Id.*

awards.The enforcement of a foreign arbitraldecision in Mongolia is regulated by the *Law on Enforcement of Court Decisions*.According to Article 7.3.3, if MINAC receivesa request for enforcement of a foreign arbitral award, MINAC will send this award decision to Mongolia'sOffice of Court Decision Enforcement, which will be responsible for processing the request and initiating enforcement procedures.[53]

According to the *Arbitration Law*, Article 42.5, the party applying for the enforcement of an arbitral award in Mongolia mustsubmit the following documents with its application: a duly authenticated original award or a duly certified copy thereof; the original arbitration agreement or a duly certified copy thereof; receipt of payment of the State Stamp Fee; and a request to enforce the arbitral award.[54]If the award is not made in the official language of the Mongolian state (i.e., Mongolian), the requesting partyshould also furnisha certified Mongolian translation of the decision in accordance with the *Arbitration Law*,Article 42.6.[55] If the Office of Court Decision Enforcement finds that the request for enforcement is reasonable, it will confirm the arbitral award and issuea writ of execution in accordance with the *Code of Civil Procedure*,Article 184.3.[56]The *Code of Civil Procedure*,Article 184.3 states that within seven days, upon examination of the arbitration award, ajudge shall confirm the award by his/her order.Once the judge has confirmed the award, he/she shall also issue a writ of execution and deliver it to the claimant and respondent within seven days.[57]

Generally, enforcement of an arbitral award ismandatory for signatory countriesof the *New York Convention*.[58] Whether a request from Mongolia for enforcement of an award outside the country is sent via MINAC or through alternative meansshouldnot influence the binding nature of thearbitral award. In other words, whether enforcement of an arbitral award is mandatory or not will not depend on the party who sentthe request to a foreign authority. However, in non-signatory countries, award enforcement will largely depend on the sender, subject matter, and more.[59] For non-signatory states, the process for sending requests for enforcement may be governed by existing bilateral treaties. If a country is not a signatory of the *New York Convention*, the requesting party needsfirst to check whether there is a bilateral treaty between the country from which the request is originating and the enforcing country.[60]In regard to Mongolian bilateral treaties, the Ministry of Justice or the Mongolian Supreme Court arethe main authorities whichhandlearbitration award requests from non-signatory states.[61] For example, the 2008 *Treaty on Judicial Assistance in Civil and Commercial Matters between Mongolia and the Republic of Korea*,Article 4.2 states that parties shall send their requestsfor legal assistance to a foreign authority through the Supreme Court of the state, andthat the Supreme Court will be the main authority to connect the requisite government agencies.[62] Although Mongolia and the Republic of Korea are both signatories to the *New York Convention*, it is a bilateral treaty similar in nature to the one above that should be referenced in the case of arbitral award enforcement in a non-signatory state.

In practice, if a party wants to enforce an arbitral award in Mongolia from a signatory nation of the *New*

[53] Law on Enforcement of Court Decisions, art. 7.3.3 (amended 2007) (Mong.)
[54] Arbitration Law, art. 42.5 (2003) (Mong.).
[55] *Id.* at art. 42.6.
[56] Code of Civil Procedure, art. 184.3 (revised 2002) (Mong.).
[57] *Id.*
[58] New York Convention, *supra* note 51.
[59] Mongolian International National Arbitration Center, http://en.mongolchamber.mn/index.php/business-services/mongolian-national-arbitration-center.
[60] Ministry of Justice, http://www.pmis.gov.mn/pmis_eng/.
[61] *Id.*
[62] Treaty on Judicial Assistance in Civil and Commercial Matters between Mongolia and the Republic of Korea(2008), *available at* http://www.mongolembassy.com/downloads/09.pdf.

York Convention*, the partymay send its request to the Office of Court Decision Enforcement by him/herselfor via MINAC. If the party wants to enforce an arbitral award in a non-signatory country of *New York Convention*, the party needs first check the existence of a bilateral treaty with that country in order to find out which authority has the power to communicate with the foreign authority responsible for enforcement.

In the case of ad hoc arbitration which occurs in Mongolia, with an award that will be enforced domestically, a similar procedure to the one described above should be followed. In the event the party against whom an award has been issued fails to comply with the arbitral award, the party seeking enforcement may submit a request to the Court of Appeals. The request for enforcement should include the original arbitral award, or a notarized copy thereof, and a receipt demonstrating the party's payment of the State Stamp Fee. These documents are to be submitted to the Court of Appeals who will thereafter issue a writ of execution to the Office of Court Decision Enforcement.

Statute of Limitations Issues

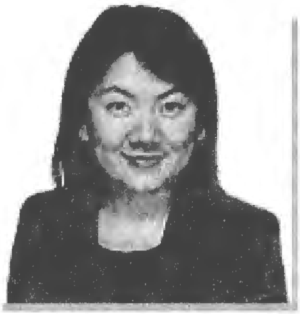
There may be questions regarding whether Mongolia's statute of limitations applies in arbitral proceedings where theparties have chosen to begoverned by the laws of Mongolia.In regard to the statute of limitations, the *Civil Code*, Article 74.1states that "the right to demand a party to take any action shall have a limitation period," unless the law specifically stipulates the limitation period is irrelevant.[63] Since the law's language includes "any action," the statute of limitations will likely include arbitration proceedings. In addition, the *Civil Code*,Article 82.4 states that "[i]f the expiration of the limitation period is justifiable, a court or arbitration body may restore it and protect the breached rights."[64] This means that, according to the provisions within the*Civil Code*, an arbitral body may restore the limitation period. Thus we can conclude that the aforementioned articles governing Mongolia's statute of limitations will apply to arbitral proceedings. For example, if a claim related to obligations is due to be performed within a fixed time, but the parties do not file a claim before the court or in accordance with the contract's arbitration clause, then after three years the claim may not be able to be pursued given that the statute of limitations period has passed.

Conclusion

Ad hoc arbitration provides parties with more independence in arbitral proceedings, including providing greater flexibility in terms of choosing tribunals or procedural rules than that found in institutional arbitration. Ad hoc arbitration also provides the parties with the ability to avoid potential biases in Mongolia's institutional arbitration. If the parties agree to commence ad hoc arbitration in Mongolia, parties may freely choose *UNCITRAL Rules*, Mongolian *Arbitration Law*, or any other foreign arbitration procedural rules. *UNCITRAL Rules* are often used in ad hoc arbitration due to their greater uniformity and legal predictability, which are in-line with global standards. If parties choose *UNCITRAL Rules*, the parties may select domestic or foreign appointing authorities, qualified arbitrators of their choice, and the preferred location for arbitral proceedings. Thus, in the jurisdiction of Mongolia, the choice of ad hoc arbitration conducted pursuant to *UNCITRAL Rules*, at the parties preferred location and in the decided upon language, may be a preferable choice for international and/or domestic parties when considering various forms of dispute resolution to govern commercial transactions within the country.

[63] Civil Code, art. 74.1 (revised 2002) (Mong.).
[64] *Id.* at art. 82.4.

TAKING SECURITY IN MONGOLIA – ISSUES AND CHALLENGES



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In recent years, the Mongolian economy has become heavily dependent on the mining sector. The development of this capitalintensive sector and its associated infrastructure requires sponsors to have access to funds. Due to the under-developed capital market with low liquidity, the vast majority of financing comes through conventional debt financing. Financing costs are comparatively high in Mongolia,where interest rates are in the double digits.

In addition, borrowers must provide an adequate level of security to ensure the repayment of funds extended by financial institutions. However, in Mongolia thepool of assets that could provide reliable and enforceable security is limited. This makes financing more difficult and less accessible tosmall and mid-sized companies. This is due to the shortcomings of the existing regulatory regime, as further discussed below.

1. Introduction

The principal form of security interest is a "pledge". Under Mongolian law, in principle it is possible to take a pledge over immovable and movable property, as well as proprietary rights such as intellectual property rights. In almost all cases, the creation of a security interest by way of entering into a relevant pledge agreement will equate to the perfection of the same. The exception is a pledge over immovable property, which is perfected upon registration with the relevant state authority.

Although it is theoretically possible to register security interests created over other assets such as movable property and shares in private companies, there are no enabling regulations governing the process for this. The Ministry of Justice is cooperating with the International Finance Corporation to introduce a new law on the registration of movable properties and proprietary rights as well as security interests created over the same, but the question remains as to whether the adoption of new law would be sufficient to provide a reliable and predictable security regime.

2. Registrable Securities

2.1.Immovable Properties (including land)

It is possible to create security over land possession rights and land ownership rights (the former may be issued to wholly Mongolian legal and natural persons whereas the latter are only issued to Mongolian natural persons) as well as overbuildings (the ownership rights over which are separate to land rights).

The registration of security interest over buildings equates to the perfection of such security interest and failure to registermeans that the security is invalid and unenforceable against a pledger. The registration system for security over immovable properties is relatively well-developed and maintained by the Mongolian Property Rights Registration Office.

However, state registration of security interests over buildings and lands is not publicly accessible and as such searchesof the same require the cooperation of the property owner.

2.2.Mineral Licenses

Under Article 51 of the Minerals Law, it is possible for banks and non-banking financial institutions to take security over mineral and mining licenses provided that this is also accompanied by the relevant documents relating thereto, such as exploration data and reports, feasibility studies, and other relevant pledgeable assets. This means that a mineral/mining license by itself is not a securable asset. The Minerals Resources Authority of Mongolia is in charge of registration.

2.3. Trademarks

Under the Law of Mongolia on Trademarks and Geographical Indications, security over trademarks is subject to registration with the Intellectual Property Office of Mongolia. Although the law appears to require mandatory registration, there are no enabling regulations detailing the registration mechanism and application procedure. From Hogan Lovells' own experience, we understand that in order to pledge trademarks a holder of the same must first have the trademark evaluated and a report commissioned. Given the early stage of practice in this field and relative absence of recognition and valuable Mongolian corporate trademarks, it remains unlikely that companies have access to significant levels of funding by way of securing their trademarks.

2.4.Vehicles

One of the most common types of movable property that Mongolian mining companies have in their possessionis vehicles and these can be substantialin value. However, it appears that the Mongolian vehicle registration system does not currently allow the registration of security over the same. Instead,as a way around this, lenders often request the transfer of ownership of vehicles into their name until the secured obligations have been fully repaid.

2.5.Shares in joint stock companies

Shares in publicly-traded companies are registered with the Securities Central Depository and Clearing House ("**SCDCH**") and it is possible to register security over such shares with the SCDCH. There is a relatively well-developed registration mechanism in place, however due to the low liquidity of shares at the Mongolian Stock Exchange, this option is not open for most companies seeking funding, as it is not particularly attractive to lenders.

2.6.Shares in private companies

One of the most common types of securable assets are shares in private companies. However, there exists no registration mechanism for shares in private companies, nor for security over the same.

In practice, the registration of a private company and its shareholders with the Legal Entities Registration Office ("**LERO**") evidences the shareholders' ownership rights over shares in such company, however no legislative act in Mongolia confirms this. Rather, the Company Law of Mongolia provides that ownership rights over shares are evidenced by a register of shares/members maintained by companies. Mongolian companies often do not generally maintain such register and as such shareholders rely on the details set out in company charters and state registration with LERO. LERO does not register security over shares in private companies and therefore lenders are left with no choice other than to rely on the contractual arrangements with a pledger.

2.7.Other assets

There is no registration system available for registration of security over other types of assets or proprietary rights.

Although technically it is possible under Mongolian law to take floating charges, there are no detailed regulations in relation to the same. Further, Mongolian companies do not maintain aregister of pledges which would evidence the existence of security interests generally.

Despite the absence of enabling regulations, there are cases where borrowershave successfully registered pledges over certain high-value movable assets and trademarks. However, such registrationsare considered to be isolated incidents and required a great deal of effort and use of connections and influence on the part at the borrowers.

2.8.Way Forward

As discussed there is no established system for registering security interests over assets other than those detailed above-mentioned. This applies to pledges of shares in limited liability companies, movable assets, receivables, and the other more general assets of companies.

The absence of a publicly searchable and established registration system makes it difficult for lenders to "get comfortable"with the risks associated with extending loans in Mongolia and therefore to provide funding. Having received the benefits of warranties and covenants under the relevant pledge agreements, lenders are left with no assurance other than relying on pledgees to comply with their contractual obligations. The lack of a registration system also makes it difficult for lawyers to opine (without substantial qualifications) on the ranking of security interests as it is not possible to confirm the existence of a prior pledge.

Overall, companies without valuable immovable properties have limited ability to raise funding from international banks who are able to provide considerably cheaper finance than Mongolian banks.

If there was sufficient support and the political will, a mandatory mechanism for the registration of security interests over most asset typescould be created without too much effort. However, such mechanism needs to gain the trust of the public by ensuring reliability and accessibility. The creation of trust is a rather more difficult process than just creating an enabling environment.

The State has several options it could consider in creating a reliable security regime. Firstly, the existing legislation on taking security could be amended so as to create a reliable registration mechanism for pledges over movable assets and proprietary rights, including shares over private companies. However, these options are not limited to passing of new laws on the registration of security interests. It would also be possible to create a self-reporting system where companies were obliged to maintain a register of security interests provided by them to lenders. Failure to maintain incorrect or false registration would have financial or other penalties. Such a self-reporting system would develop reliability and trustworthiness and would beless costly for the State in terms of creation and enforcement.

Such registration systemswould provide assurance and comfort for lenders in extending loans facilities to Mongolian companies, and may potentially reduce financing costs. The increased pool of assets over which reliable security interests can be given wouldprovide more funding opportunities to Mongolian companies, which in turn should result in business growth and the economic development of Mongolia.

INTERNATIONAL LEGAL PERSONALITY OF INTERNATIONAL ORGANIZATIONS: INTERNATIONAL LAW PERSPECTIVE

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Abstract

In traditional concept of international law, States were only subjects of international law. Accordingly, the criteria applicable to subject of international law were mostly dedicated to States. This concept dominated until the end of the 19th century. In the beginning of the 20th century, new actor as international organization appeared institutionally in international relations. Naturally, the requirements of international life have influenced the development of international law, and the increasing cooperation among States has led to appear non-state actors in international plane.

Basically, this article is intended to introduce general framework of international legal personality of international organization as one of the current main actors in international law. This is the fundamental issue in connection with the existence of international organization in international relations. In this article, I will analyze three theories regarding international legal personality of international organizations and the criteria of international legal personality (in particular, those of international organizations) in order to answer the questions of whether international organizations possess international legal personality under international law or whether international organizations can exercise their functions without having international legal personality.

Introduction

The legal subjects in any legal system are not necessarily identical in their nature or in the extent of their rights, and their nature depends upon the needs of the community. Throughout its history, the development of international law has been influenced by the requirements of international life, and the progressive increase in the collective activities of States has already given rise to instances of action upon the international plane by certain entities which are not States.[1] In principle, international organizations[2] are quite different from States because of the

[1] ICJ Advisory opinion, *Reparation for injuries suffered in the service of the United Nations* (April 11th, 1949), p.178. Available at http://www.icj-cij.org/docket/files/4/1835.pdf.

[2] There is no generally-recognized definition on international organization. In a broad sense, the term *international organization* covers intergovernmental organizations, international non-governmental organizations, international tribunals, international public corporations, and even multinational enterprises established by the law of the particular State. In a narrow sense, it means intergovernmental organizations. In this respect, Vienna Convention on the Law of Treaties (1980) provides that international organization is intergovernmental organization (Article 2 (i)). The former is a quite disputable issue among international law scholars. Although the latter expresses traditional concept of international organizations in international law, in fact, it cannot fully encompass diversity among international organizations.

fact that they do not possess a general competence and have been established in order to exercise specific functions.[3] States possess common rights and duties recognized by international law whereas the rights and duties of international organizations depend upon their purposes and functions expressed or implied in their constitutions and developed practice in this matter. For this reason, the fact that international organization is an international legal person does not mean that it is in the same position as a state in international law. Therefore, to be an international legal person means only to be capable of bearing rights and duties.[4]

This short article seeks to answer two basic questions: whether international organizations possess international legal personality under international law or whether international organizations can exercise their functions without having international legal personality. In order to accomplish this purpose, main theories for international legal personality of international organizations, and the general and specific criteria applicable to international legal personality of international organizations will be briefly explored in this article. Consequently, that international legal personality is an indispensable feature for existence of international organizations in international relations will bedetermined. In addition to this, some questions that need to be answered will be arisen. Substantially, this article focuses on only general framework for international legal personality of international organizations. I will consider domestic legal personality and legal responsibility of international organizations separately in my next articles.

[3] This is called as *'the principle of specialty"*. It means international organizations are established in order to exercise specific functions. See the UN, International Law Commission, *Draft Articles on the Responsibility of International Organizations, with commentaries* (2011), p.3

[4] Henry G. Schermers and Niels M. Blokker, *International Institutional Law: Unity within Diversity* (5th revised edition; Leiden, Boston: Martinus Nijhoff Publishers 2011), p.993

Why is international legal personality important to international organizations?

The priority questions in this regard are whether international organizations possess international legal personality[5] under international law or whether international organizations can exercise their functions without having international legal personality[6]. In this respect, it is deemed an entity that is not a "subject of international law" or an "international legal person"[7] is not able to be a party to treaties, present claims against other international persons, possess other international rights and duties, or otherwise exist with relative autonomy in the legal sphere.[8] There are fundamental three theories regarding international legal personality of international organizations.

The first theory was generally developed by socialist scholars, such as G. I. Tunkin[9] and etc.,. This theory assumed that constitutions (in other words, headquarter agreement) of

[5] German legal scholar Gottfried Wilhelm Leibniz first used the term ***international legal person*** (persona jure gentium) in his *Codex Iuris Gentium diplomaticus* (1693). See J.H.W. Verzijl, *International Law in Historical Perspective, Volume II: International Persons* (1969), at 2, and Janne Elisabeth Nijman, *The Concept of International Legal Personality: An Inquiry Into the History and Theory of International Law* (2004), p.29

[6] C.F.Amerasinghe, *Principles of the institutional law of international organizations* (2nd revised edition), Cambridge University Press 2005, p.67

[7] According to the treatises of most legal scholars (Jose E. Alvarez, and Henry G. Schermers and Niels M. Blokker, etc.,), the terms *"subject of international law"* or an *"international legal person"* are used interchangeably.

[8] Jose E. Alvarez, *International Organizations as Law-makers*, Oxford University Press 2005, p.129. See also Henry G. Schermers and Niels M. Blokker, *International Institutional Law: Unity within Diversity* (5th revised edition; Leiden, Boston: Martinus Nijhoff Publishers 2011), p.985 and C.F.Amerasinghe, *Principles of the institutional law of international organizations* (2nd revised edition), Cambridge University Press 2005, p.68

[9] See J.I. Tunkin, *The Legal Nature of the United Nations*, 119 RdC (1966 III), pp. 20-25

international organizations expressly stated that these organizations have international legal personality. Henry G. Schermers and Niels M. Blokker argued that such provisions oblige the members to accept the organization as a separate international person, competent to perform act that under traditional international law could only be performed by states.[10] Thus, according to this theory, the most important precondition for possessing international legal personality under international law by the particular international organizations are the provisions on the international legal status of that organization in its constitution. However, in fact, most constitutions contain no explicit such provisions. Indeed, in a view of the first theory, the question to how to resolve international organizations in which have no expressed provisions on having international legal personality of these organizations in their constitutions remains uncertain.

The second theory emphasizes the concept of "objective legal personality of international organizations".[11] Objective legal personality contains two different arguments. Firstly, international organization is a separate legal person from its constituencies, such as member States and Organizations, or it does not depend on the (subjective) will of its members.[12]Secondly, international organization has the objective legal personality in its relation with non-Members[13].Objective legal personality was first expressed in the case of *Reparation for Injuries suffered in the service of the United Nations* resolved by the International Court of Justice (ICJ) in 1949.[14] The ICJ held that the United Nations possesses an objective legal personality distinct from that of its members in this case. As the second argument, main ground of its advisory opinion is that fifty States, representing the vast majority of the members of the international community, had the power, in conformity with international law, to bring into being an entity possessing objective international personality and not merely personality recognized by them alone, together with capacity to bring international claims.[15] However, the issue of how many member States at a minimum are required to international organization with objective personality was not an issue before the Court and was not decided by it.[16]

In this case, the court concluded that:

In the event of an agent of the United Nations in the performance of his duties suffering injury in circumstances involving the responsibility of **a Member State and a State which is not a member**, the UN as an Organization has the capacity to bring an international claim against the responsible *de jure* or *de facto* government with a view to obtaining the reparation due in respect of the damage caused to the UN.[17]

[10] Henry G. Schermers and Niels M. Blokker, *International Institutional Law: Unity within Diversity* (5th revised edition; Leiden, Boston: Martinus Nijhoff Publishers 2011), p.988

[11] Main representative of this theory is Finn Johannes Seyersted. He wrote several books on international personality of international organizations, such as *Objective International Personality of Intergovernmental Organizations* (published in 1964), *The Legal Nature of International Organizations* (published in 1982), *Common Law of International Organizations* (published in 2008).

[12] Henry G. Schermers and Niels M. Blokker, *International Institutional Law: Unity within Diversity* (5th revised edition; Leiden, Boston: Martinus Nijhoff Publishers 2011), p.989

[13] Nneoma Chigozie Udeariry, *To What Extent do International Organizations Possess International Legal Personality?* (September 15, 2011), p.11. Available at SSRN: http://ssrn.com/abstract=2052555 or http://dx.doi.org/10.2139/ssrn.2052555

[14] Ibid., p.12

[15] ICJ Advisory opinion, *Reparation for injuries suffered in the service of the United Nations* (April 11th, 1949), p.187

[16] C.F.Amerasinghe, *Principles of the institutional law of international organizations* (2nd revised edition), Cambridge University Press 2005, p.87

[17] ICJ Advisory opinion, *Reparation for injuries suffered in the service of the United Nations* (April 11th, 1949), p.185

According to the third theory, international organizations are international legal persons, explicitly (their constitutions stipulate that they have international legal personality), or implicitly (in reality, international organizations could not exercise and enjoy, functions and rights, including conclude treaties, exchange representatives and mobilize international forces, without possessing international personality).[18] Possessing legal personality is an indispensable prerequisite for the existence of international organizations in international relations in idea of this theory. Currently, the third theory may be the most recognized idea of legal personality of international organization.

Generally, these three theories illustrates that international organizations possess international legal personality and they cannot accomplish their purposes and exercise their functions without having international legal personality. Nonetheless, legal status of international organizations are not the same as States. Purposes and functions of international organizations are limited by their constitutions. For this reason, the criteria applicable to international organizations are differentiated from those of States. Article 1 of Montevideo Convention on the Rights and Duties of States (1933)[19] states: "the State as a person of international law should possess the following qualifications: a) a permanent population; b) a defined territory; c) government; d) capacity to enter into relations with the other States. Obviously, these criteria are not applicable in determination of legal personality of international organizations. This situation was led to create new criteria for international organizations. In Reparation case, the ICJ held that the UN as international legal person is capable of possessing international rights and duties, and has capacity to maintain its rights by bringing international claims.[20] Although having capability of possessing international rights and duties, and capacity to maintain its rights by bringing international claims should be common criteria for all international legal persons, some scholars had determined specific requirement for international organizations. For example, the detailed criteria for legal personality of international organizations were determined by Professor Ian Brownlie. He suggested that the following criteria are required to having legal personality by international organizations:

a) a permanent association of states, with lawful objects, equipped with organs;

b) a distinction, in terms of legal powers and purposes, between the organization and its member states;

c) the existence of legal powers exercisable on the international plane and not solely within the national systems of one or more states.[21]

Professor Brownlie's such criteria are not only applicable in international law, but also in domestic law.

Conclusion

This article examines only international legal personality of international organizations. It does not cover domestic legal personality and legal responsibility of international organizations. By virtue of examining three theories on international personality of international organizations, it is clear that international organizations possess international legal personality under international law or international organizations can exercise

[18] See Henry G. Schermers and Niels M. Blokker, *International Institutional Law: Unity within Diversity* (5th revised edition; Leiden, Boston: Martinus Nijhoff Publishers 2011), p.989

[19] This Convention was signed at Montevideo, Uruguay, on December 26, 1933, during the Seventh International Conference of American States. The Convention may be used as norms of customary international law.

[20] ICJ Advisory opinion, *Reparation for injuries suffered in the service of the United Nations* (April 11th, 1949), p.179

[21] Ian Brownlie, *Principles of Public International Law*, 4th edition, Oxford University Press, 1990, p. 681-2

their functions by the way of possessing international legal personality.

International organizations are subject to the principle of specialty. Therefore, international organizations should possess international legal personality when they exercise their functions in order to fulfill their purposes in their constitutions. Nonetheless, there are several priority questions that need to be answered due to the fact that diversity of international organizations is getting more difficult to determine whether international organizations have international legal personality. Defining international organization is the first considerable question in this regard. Next question is what kind of criteria (common or specific) are applicable to determining international legal personality of international organizations.

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ICELAND'S MELTDOWN AND REVIVAL: A LESSON IN REBOUNDING

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Introduction

"Iceland's collapse even today should be sending out warnings to countries with over-extended banking sectors, such as Denmark and Sweden[1]".

In the autumn of 2008, Iceland's three major banks, Glitnir, Landsbanki and Kaupthing were overwhelmed by the failure of the Lehman Group and the resultant global financial crisis. The Icelandic government first stepped in to nationalize these three banks. Then it transferred "good" assets to three successor banks and although the cashpoint machines kept humming, the Icelandic economy ground to a halt. In days, the complex business empires and household names underpinning that economy, such as Baugur and Bakkevoor came under pressure and Iceland became a pariah in global financial circles.

So, what lessons can be learned from Iceland's experience?

Boom times and before

Iceland is a small country with a population today of 325,000. Iceland'sprincipal natural resources are sheep, fish, thermal energy, and aluminum. Following the occupation of Denmark by Germany in 1940, the Icelanders severed their ties with the Danish Crown. Barely a month after that occupation, the British army took over Iceland and the country developed as a major staging post. Following the end of World War II, Iceland was a nation with strong currency reserves. These reserves developed and consolidated very largely through the construction of a major American airbase at Keflavik, now the site of Reykjavik international airport.

Iceland developed into a state controlled and socialist economy in the years following World War II. A small number of long established and wealthy families gained control over the island's transport routes, at the heart of which lay the Eimskip Shipping Company, formed in 1914. The two principal families within this group – which was known as the "Octopus" – were the Engey family and the H. Bens clan. These and the other families within the "Octopus" were not a formal group. They operated informally but wielded great, albeit covert, influence over many aspects of Icelandic trading activity.

All that began to change from 1991 when the Icelanders elected the former major of Reykjavik, David Oddsson, as their prime minister. Oddsson was a staunch Thatcherite. He came to power on a mandate of privatising and opening up the Icelandic economy. Oddsson set about this task by persuading the Icelanders that their country had diminished in significance and needed a radical overhaul if it was to develop and

[1] Page 6, *Meltdown Iceland* – Roger Boyes 2009 – Bloomsbury Publishing

thrive in the modern trading environment.

By October 2008, the Icelandic economy was at the height of its powers. The three chief banks, Glitnir, Kaupthing and Landsbanki had between them funded an explosion of investment within the local and overseas economies. In the United Kingdom, Icelandic businesses – such as Baugur – acquired substantial stakes in a number of iconic UK retailers. The highest profile examples were House of Fraser, Moss Bros and the flagship toyshop, Hamleys. The West Ham football team also fell into Icelandic hands. The purchase and sale of fishing quotas made dollar millionaires of many ship owners. These new entrepreneurs had to a large extent purchased substantial properties and premium motor vehicles, funded by foreign currency mortgages. That funding was storing up a time bomb, as the earnings and interests of these dollar fish quota millionaires and business magnates were to a large extent generated – and measured – by reference to the Icelandic Kroner.

Glitnir, Kaupthing and Landsbanki were privatised. Landsbanki was taken over by the Independence Party loyalist, Bjoergylfur Gudmundsson. Kaupthing fell to a group of investors led by Olafur Olafsson, with affiliations to some of the country's more progressive politicians. These banks all lent to each other, while Glitnir in particular lent to the purchasers of fishing quotas. Many of the acquisitions of the UK businesses referred to above were funded by these three banks. When it came to unravelling their affairs, valuing and providing for the fishing quota transactions within Glitnir proved to be an especially challenging aspect of the bank reconstruction process.

It is fair to say that by the end of 2007, many City lawyers and other advisors coveted these financial institutions and the management of their loan books as clients. Hindsight is indeed a wonderful thing.

The Gathering Storm

By 2005, Icelandic credit was growing at in excess of 30% annually. The current account deficit had expanded to 15% of GDP in the same year and net external debt had reached more than 400% of current external receipts. Faced with an urgent need to raise capital, Glitnir, Landsbanki and Kaupthing moved into the British market. Each offered to prospective depositors interest rates that looked – and which ultimately turned out to be– too good to be true. Kaupthing Bank had purchased Singer and Friedlander, a long established, British bank. Numerous major British institutions – not to mention many individuals – then went on to deposit material sums with the London banking operations of the Icelandic banks. These included Cambridge University - J11 million, Oxford University - J30 million and 116 local authorities. These local authorities, between them, deposited J858 million in Icelandic banks. All these depositors had been lured by the favorable interest rate terms made available to them.

Meltdown

In autumn of 2007, the British bank, Northern Rock, had fallen into difficulty after becoming unable easily to raise finance on the money markets. Three BNP mortgage vehicles also encountered difficulties and BNP Paribas stopped withdrawals from them, citing a "complete evaporation of liquidity" as the reason for doing so. In March 2008, JP Morgan bailed out the American bank, Bear Stearns. Far worse was to come when on 15 September 2008, the US investment bank, Lehman Brothers entered into Chapter 11 bankruptcy proceedings in the US and equivalent insolvency procedures in numerous other jurisdictions. Those proceedings included the administration of Lehman Brothers International Europe, the principal English Lehman group company.

Crisis

The failure of the Lehman Group in September 2008 produced cataclysmic reverberations within the Icelandic banking system. In September 2008, Glitnir had sought US$820 million of liquidity. On 28 September 2008, it had been proposed that the Icelandic Central Bank would inject US$750 million into Glitnir in return for a 75% stake. At the same time, Landsbanki sought a US$200 million liquidity loan. That was turned down by the Central Bank. On 5 October 2008, the Icelandic government passed the Emergency Powers Act – Act 129/2008. On 7 October 2008, the Icelandic government nationalised Glitnir and Landsbanki.

That nationalisation marked the beginning of the real crisis in Iceland. The Icelandic government made clear that it would not stand behind the liabilities of these banks to overseas depositors. It also became apparent that unlike the governments in Ireland and the UK, the Icelandic government would be unable to stand fully behind the rights and liabilities of Glitnir and Landsbanki, let alone Kaupthing and other financial institutions. There followed tense exchanges between the Icelandic government and the British chancellor, Alastair Darling. The upshot of those exchanges was that the Icelandic government made clear that it lacked the means of supporting the liabilities to overseas depositors of Glitnir and Landsbanki. Instead, the government would guarantee only these banks' liabilities to Icelandic depositors.

The reaction of the British government was immediate – and arbitrary. It decided that Heritable Bank, a subsidiary of Landsbanki was no longer able to meet its liabilities. Heritable – along with Kaupthing Singer & Friedlander, the UK subsidiary of Kaupthing Bank, went into administration. On the same day, Alastair Darling passed the Landsbanki Freezing Order 2008. That Freezing Order applied to both the UK assets of Landsbanki and those belonging to the Icelandic Central Bank and the Government of Iceland. The UK government had made that freezing order in reliance on anti-terrorist legislation.

Although these actions were arbitrary and difficult to justify legally, they further underlined the political difficulties facing Gordon Brown's government as a result of the Icelandic collapse. Those difficulties stemmed in turn from the extent to which private individuals and public institutions faced the destruction of their finances through the failure of Icelandic institutions that had promised them interest rates that had indeed proved too good to be true.

Over the ensuing months, the sanctions were progressively removed and on 24 October 2008, the Icelandic government, on legal advice, formally asked the IMF for help. That resulted in an IMF loan to Iceland of US$2.1 billion. On 15 November, Iceland announced that it would comply with the EU Deposit Guarantee Scheme directive guaranteeing compensation for up to 20,877 for each Icelandic savings account. The arrangement was that Britain would compensate 300,000 depositors in Iceland and Iceland would reimburse Britain following the making of the IMF loans referred to above.

In the meantime, the Icelandic government realised that it would be unable to underwrite the liabilities of Glitnir, Landsbanki and Kaupthing. It therefore used the emergency powers legislation to take control of each institution. The result was that the Icelandic financial services authority (the "FME") established successor banks to each of Glitnir, Kaupthing and Landsbanki. These "new banks" contained within them the domestic operations of their predecessors together with local Icelandic deposits.

The "old" banks were the insolvent shells of Glitnir, Landsbanki and Kaupthing. These banks contained within them assets and liabilities in foreign branches and subsidiaries, together with derivative transactions. Five member resolution committees were appointed to each of Landsbanki and Glitnir on 7 October 2008. The following day, resolution committees were appointed to Kaupthing Bank.

Under the emergency powers legislation, the "old" banks gained the benefit of a moratorium, akin to that operating in US or UK bankruptcy or administration proceedings. That moratorium prevented litigation against the old banks. It also created time for the relevant stakeholders to hammer out a composition which lead to the successor banks paying the shells of Glitnir, Landsbanki and Kaupthing for the assets transferred to them. The payments so made were then to be applied in compositions – creditor compromises – to give a return to the bondholder and other creditors of the "old" banks. In many ways, this process is similar to the bail-in procedures that are currently in negotiation between the European Union and European Union governments pursuant to the Bank Resolution and Recovery Directive.

PICKING UP THE PIECES

The use of anti-terrorist legislation to freeze the UK assets of the Icelandic government and banks polarised opinion. It also acted as a clarion call to the Icelandic government. The result was that Hogan Lovells and a number of Icelandic law firms were appointed to act as legal and financial advisors. Between October 2008 and the beginning of 2009, we provided advice to the Icelandic government on the effect of the Landsbanki freezing order together with the potential merits of seeking a judicial review of this order and possible damages claims against the British government.

Hogan Lovells also provided advice on the operation of inter-bank payments in relation to the "new" banks. We also assisted the government in addressing the inter-relationship between the Icelandic resolution committee process, Icelandic moratorium (bankruptcy) proceedings for the "old" banks and the effect of those proceedings on the assets of the "old" banks outside Iceland. Hogan Lovells evaluated the legitimacy under EU law of various Icelandic proposals to pay compensation to overseas depositors with Kaupthing, Glitnir, Landsbanki and their subsidiaries.

The result of this work was that by the beginning of 2009, the Icelandic government was in a position to restructure its banking system. The government appointed a former Scandinavian banking executive to supervise that work. Once again, the government tendered for credible international advisers. Both Hogan Lovells and Hawkpoint Partners were appointed to provide legal and financial advice on the recapitalisation process.

Part of our work involved us assisting the resolution committees for each of the "old" banks, Glitnir, Landsbanki and Kaupthing in deriving value from the various successor banking institutions for the assets transferred to them. That process involved working with the creditors' committees of each "old" bank and representatives of the UK depositors who had lost out following the collapse in October 2008. The most difficult aspect of the work was agreement of the basis of the further valuations carried out by Oliver Wyman to underpin and as appropriate correct the preliminary valuations carried out at the time of the establishment of the "new"banks in 2008. The intention was that the new banks would pay the resolution committees of Glitnir, Landsbanki and Kaupthing for the difference between the value of the assets and liabilities transferred to them as verified by Oliver Wyman and the preliminary valuations undertaken in 2008.

The payment mechanism ultimately agreed led to the issue of bonds by the "new" banks together with options for the resolution committees of the "old" banks to acquire control of each "new" bank. The result of that process was to be the creation of a fund that could be distributed to the creditors of the "old" banks through the use of Icelandic composition proceedings.

Outcome

On the surface, Iceland's economy appears to have recovered. The fact that the currency is not linked to the Euro means the economy has recovered faster than many of its European cousins. Unemployment has fallen to 4% and Iceland's cashpoint machines continue to function. On the debt side, however, capital controls remain in place. The "old" banks have yet to resolve the claims of their creditors, on account of the valuation issues discussed earlier in this note. Additionally, output in Iceland is around 10% below its pre-crisis peak. Inflation stood at 2.4% in May 2014. Furthermore, the Kroner is now at a rate of around 157 Kroner per Euro compared with an average rate of 88 Kroner per Euro in 2007, a year before the financial collapse. In short, it remains to be seen whether Iceland is now on the road to a full recovery. The one certainty, however, is that the easy credit and tightly inter-related business conglomerates that contributed so greatly to Iceland's prosperity and ultimately its downfall are now a shadow of their former selves.

Lessons Learned

Certainly, there is no "one size fits all" solution when a country encounters economic difficulties. However, Iceland's experiences can be useful in noting potential danger signals which a government can then meet head-on. In Iceland's case, foreign currency mortgages obtained in the United Kingdom were a time bomb that ought to have been defused early on rather than left to "wishful thinking." Certainly, if a proposal offers rewards that are "too good to be true," costly experience shows that such rewards are illusory and remedial measures painful if not taken promptly. Once the Icelanders realized the urgent need to raise capital in a weakened economy, they exacerbated the problem by moving into the British market offering overly optimistic interests to potential depositors.

When the Icelandic government called upon Hogan Lovells for assistance, there was no text book solution. We performed the role of an interlocutor among many stakeholders and created solutions based upon local and English law as well as international banking practices. In many cases, we were pioneering into an area where Icelandic law often did not present immediate solutions and we needed to come up with creative ideas in order to meet the emergency at hand. We did, and it looks like Iceland is well on the road to recovery.

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MEMORANDUM OF ADVICE TO THE MINISTRY OF JUSTICE:ON THE CRIMINAL LIABILITY OF CORPORATIONS FOR DEATH AND INJURY IN THE WORKPLACE UNDER MONGOLIAN LAW[1]

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Between 2006 and 2010, an average of 100 Mongolian workers per year died as a result of workplace incidents. Another 2000 workers on average per year lost the ability to work due to occupational illness or incidents. (statistics cited in "11th Report on Human Rights and Freedoms in Mongolia", Human Rights Commission of Mongolia, Ulaanbaatar, 2012, p.52)

Introduction:

The safety of Mongolian workplaces is not only good for business, but is also a recognized Human Right enshrined in the Constitution: it asserts a "Right to...favorable conditions of work." The Government has approved a national programme "To improve occupational health and safety." (byresolution 75 of 2005) . The programme aims to introduce a culture of prevention regarding occupational health and safety, reducing occupational illness and production injuries, creating all the necessary conditions to protect health and life of employees at work, and *improving the legal environment* to protect workers from occupational hazards. The State Great Hural adopted the law on Occupational Safety and Health on 22 May, 2008 ("*11th Report on Human Rights and Freedoms in Mongolia*", Human Rights Commission of Mongolia, Ulaanbaatar, 2012, p.50, my emphasis).

Despite introducing Labor inspection reforms in 2010, there are businesses and organizations which lack adequately developed labor relations. An examination by the Ministry of Social Welfare and Labor and the General Agency for Specialized Inspection revealed that a number of businesses have "failed to create an enabling environment for occupational health and safety." (*11th Report on Human Rights and Freedoms in Mongolia*", Human Rights Commission of Mongolia, Ulaanbaatar, 2012, p.51).

The statistics incorporated in the *11th Report* of the Human Rights Commission of Mongolia demonstrate the unacceptably high death and injury rate among Mongolian workers. As industries such as mining and construction continue to develop apace, the legislature's focus upon ensuring workplace safety ought to be even more vigilant.

The above statistics (at *11th Report*, p53) include the most severe breaches of occupational safety regulations. According to the inspections and research results conducted over recent years large companies with foreign investments like Rio Tinto and Energy Resources adhere to international safety standards, whereas small businesses by and large, fail to

[1] The author wrote this comment when he was a visiting scholar in the National Legal Institute (July 21, 2014- August 22, 2014).

Year	2006	2007	2008	2009	2010	
Annual Averages						
Number of workers	460	369	671	410	398	462
Loss of Life	123	92	152	53	80	100
Serious injury	162	131	269	181	141	177
Minor injuries	160	138	241	179	177	179

comply with them. (at *11th Report*, p.54). However workplace deaths and injuries occur in all organizations, large and small. The law on occupational health and safety should apply equally to all corporations employing workers whatever the size and complexity of the commercial operation.

Due to the significant increase in mining and construction in Mongolia in recent years, the Human Rights Commission concluded that "it has become imperative to refine the relevant laws and regulations regarding occupational safety and health, enhance State's control over law implementation, improve the legal environment regulating the provision of compensation to workers who lost their ability to work...Furthermore, *it is necessary to tighten the responsibility and accountability of employers* and enhance the role and responsibility of State control institutions in ensuring strict adherence to standards relating to occupational health and safety." (*11th report*, p58, *my emphasis).*

In this memorandum, it is contended that these laudable aims and objectives can, and should, be met with the implementation of legislation designed to render corporations criminally liable for the deaths and injuries of its workers, where the corporation itself has displayed gross negligence regarding the safety of its deceased or injured worker. This paper seeks to discuss the approaches that may be adopted in sheeting home criminal responsibility to corporations, and the rationales for doing so.

Before moving to discuss the approach to legislative change required by the introduction of criminal liability for corporations, it is necessary to review, in short compass, the current legal framework regulating workplace health and safety, and its relationship to the Criminal law of Mongolia.

Mongolian Labor Safety and Hygiene Law

In Mongolia, the law regulating safety in the workplace since 22 May, 2008 is the *Labor Safety and Hygiene* Law. It makes no reference to the criminal liability of bodies corporate. Can this legislation be rendered more effective by extending to corporate entities criminal liability in certain circumstances for the death or serious injury of its workers? Or should there be a separate offence of, for example, corporate manslaughter? Arguably, there is an important deterrent value in extending to a corporation criminal responsibility for serious breaches of the work safety law, or for gross negligence, which results in injury or death.

In this paper, I will compare the Mongolian legislation to the approach taken in Victoria, Australia and Great Britain, discuss the rationales for introducing criminal corporate responsibility in Mongolia, and the possible approaches that might be adopted in implementing such legislation in the Mongolian legal system.

The Mongolian *Labor Safety and Hygiene* law has as its stated purpose to "regulate the relations with respect to maintain safety and hygiene requirements, and standards of state organizations management, inspector system and workplace, develop the condition for the citizen for working in a healthy and safe environment" (Art. 1.1). Chapter Two provides for safety and hygiene standards to be established. Chapter Three sets out the rights and responsibilities of workers, including the right to work in a workplace that meets labor safety and hygiene requirements (Art. 1.8.1.1). Chapter Four sets up organizations at various levels of government which are tasked with the responsibility of implementing the labor safety and hygiene policies. It sets up institutions at all levels of government from Parliament (Art. 21) through to Aimag, Soum, Capital and District Citizen's representative Meetings (Art. 24) and Governors (Art. 25).

Chapter Five requires the Director/ owner or employer of business entities and organizations to be responsible for maintaining labor safety (Art. 27.1) with the employer's rights and responsibilities set out in Art.28.1. Chapter Six imposes certain requirements upon employers in the event of an industrial accident or acute poisoning (Art. 29).

Chapter Seven provides for the various levels of government and business to implement labor Safety and Hygiene law (Art. 32). Provision is made for State Inspectors on labor and hygiene, providing them with a range of powers including terminating the business of an employer who violates the labor safety and hygiene legislation on several occasions (Art.33.4.9).

Finally, Chapter Eight sets out the penalties for the violation of the Labor and Hygiene legislation. A State Inspector can impose an administrative fine on an employer if the industrial accident or poisoning occurred due to the fault of the employer (Art. 36.1). A judge or State Inspector has the power to impose a larger fine if the industrial accident or poisoning occurred on two or more occasions. Higher fines may be imposed by a judge or safety inspector if the organization does not maintain labor safety and hygiene requirements where there is joint ownership and use of buildings and facilities (Arts. 36.4 & Art 8.1). A judge or State Inspector also has the power to fine officials and organizations if they do not give permission to install appropriate safety equipment.

Therefore, where a death occurs due to a violation of the Labor Safety legislation, the only penalty imposed on an organization is an administrative penalty being a fine of a mere 200 – 250,000 tugrugs; and only double that if the industrial building and facilities where the death occurred was jointly owned. If there is more than one industrial accident resulting in death, an organization may be fined only 1,500,000 – 3,000,000 tugrugs. These fines bear no relationship to the degree of negligence that caused the death or injury. Nor is there any account taken of the size and structure of a corporation which may be responsible for a death or injury. As these fines are regarded as administrative fines only, significantly, they do not carry the stigma of a criminal conviction.

The principles of punishment that apply in the criminal law- such as general deterrence and specific deterrence – are not expressly taken into account under the *Labor and Safety Law*. Other punitive measures that might deter other corporations from failing to properly ensure workplace safety are adverse publicity orders and orders requiring improvements to be made. These penalties arise from invoking criminal sanctions against corporations- they are not to be found in the current law in Mongolia either in the Labor safety legislation or in the *Criminal Code*. The *Criminal Code* of Mongolia is the repository of criminal liability of natural persons, and in very limited circumstances, of bodies corporate. Under the proposed *Criminal Code* amendments, the only circumstances under which a corporation can be criminally liable is in relation to Terrorism offences (Article 178.2) and Money Laundering (Article 166).

Before turning to the manner in which criminal liability might attach to corporations for serious breaches of Labor safety laws, I will discuss the approaches taken in Victoria, Australia, and in the United Kingdom.

Occupational Health and Safety Act, 2004 (Victoria)

In Victoria, Australia, labor safety laws are governed by the *Occupational Health and Safety* Act, 2004. That legislation is similar in many respects, both in structure and substance, to the Mongolian *Labor Safety and Hygiene* law. Part 1 of the Victorian legislation sets out the objects of the Act, *inter alia*, to "secure the health, safety and welfare of employees and other persons at work and to eliminate the risks to the health and safety of employees and other persons at work." In the definition section of the Act, references to a "person" includes both a natural person and a body corporate (s.5). Consequently, its scope for operation is wider in that respect than its Mongolian counterpart.

The Act imposes duties on 'persons', including corporations, to require that corporations have systems in place that ensure, and promote, health and safety in the workplace. As with the equivalent Mongolian laws, the Victorian Act also sets out the duties of employers to employees (section 21), and the duties of employees (section 25). Penalties attaching to the breach of duties by employers are expressed to apply to (i) a 'natural person' and (ii) a 'body corporate'. Typically, the maximum fine specified for a body corporate is *at least five times* the amount to which a natural person is liable.

It is an offence under the Victorian Act to "recklessly engage in conduct that places another person in danger of serious injury"- this attracts a maximum fine of A$260,000 (453,112,256 tugrugs) for a natural person (or up to 5 years' goal), or, for a body corporate, it attracts a maximum fine of A$1,323,000 (T 2,290,456,756 tugrugs). The duties of employers to consult with employees (part 4) in the Victorian act is very similar to the provisions on that matter in the Mongolian legislation. In anticipation of an investigation, after an incident resulting in death, the site where it occurred must not be disturbed, or contaminated, until an Inspector arrives to investigate. Another feature that is similar to the Mongolian law, is the requirements that employees be organized into work groups to represent employees on work safety issues. Another common aspect is the appointment of safety inspectors (Part 9) appointed to enforce the provisions of the legislation. They have the power to enter a workplace, inspect things and documents and also to seize anything or document that may be evidence of an offence against the Act (section 99).

Although there is a power under the Victorian law to inspect documents, does a corporation, like a natural person, have a right to silence? In other words, can it exercise a privilege against self-incrimination by preventing documents in its possession being used as evidence against it in a criminal proceeding? The power to require a corporation to produce documents which may incriminate itself came under scrutiny in the High Court of Australia in *Environment Protection Authority v Caltex Refining Co Pty Ltd* (1993) 178 CLR 477, which decided that, unlike a natural person, a corporation is not entitled to exercise a privilege against self-incrimination. In other words, a corporation cannot rely upon a 'right to silence' as could a natural person when faced with questioning as a suspect in a criminal proceeding. If required to do so, a corporation must produce documents and other things which may provide evidence against the company of the crime as alleged. It should be noted that the *Criminal Procedure Law of Mongolia,* Article 13.2 states that the Presumption of Innocence applies to all suspects and defendants. To avoid the problems raised in *EPA v Caltex*, it would be appropriate to amend Article 13.2 to exclude corporate suspects and corporate defendants from its operation. In other words, when charged with a criminal offence, any amendments to Mongolian law should not allow bodies corporate to rely either on the right to silence or on the presumption of innocence.

After an injury or death is investigated by a safety inspector (who has taken witness statements, seized documents, taken photos and obtained other evidence as required by the investigation), under the Victorian law, legal proceedings may be commenced in court (section 130) *either* by (i) a safety Inspector or (ii) for indictable (serious) offences, the Office of Public Prosecutions (i.e. The office which is responsible of all criminal prosecutions of serious offences in Victoria).

The existing *Criminal Procedure Law* in Mongolia appears to be well suited to carrying out investigations against corporate defendants. Articles 29, 30, 183, and 193-195 set out the powers of a procurator (defined in Article 5.1.7.-as a prosecuting party) and also the powers to carry out Investigations by a group of investigators, Heads of Inquiry and Investigative agencies. These Articles, collectively, provide a sufficient legislative basis for investigating corporate criminal activity. In practice, it would be important for procurators and investigators to work closely with safety inspectors in order to properly gather and assess the evidence relating to a workplace death or injury.

What conduct, or omission, is deemed to be that of the 'body corporate'? For the purposes of the Victorian legislation, any conduct engaged in on behalf of the body corporate by an employee, agent or officer of the company acting within the scope of his or her employment or within his or her authority is deemed to be conduct also engaged in by the body corporate (section 143). It should also be noted that Government and semi-government corporations are also subject to the provisions of the Victorian *Occupational Health and Safety* Act, 2004.

Both the Victorian and Mongolian legislation give inspectors the power to prohibit an activity in the workplace where there is a reasonable belief that the activity involves an immediate risk to the health or safety of a person (i.e. section 112 and Article 33.4.10).

In Victoria, apart from prosecutions arising from the *Occupational Health and Safety* Act, 2004, a body corporate may be charged with offences arising from the *Crimes* Act, 1958 (Vic), or the common law. Such offences may include manslaughter and negligently causing serious injury. When these offences are charged against a natural person, they require proof of a particular state of mind. What is the "mind' of a corporation, and how is it to be proven? Generally, criminal liability can be sheeted home to a corporation only upon proof that what is done (or omitted to be done), and the mental state with which the act was done (or omission made), are within the scope of the authority conferred by the corporation upon the person or persons on whose act, omission, or state of mind the corporations criminal liability is said to depend. (*Environment Protection Authority v Caltex Refining Co Pty Ltd*(1993) 178 CLR 477, per Mason CJ. And Toohey J.) This traditional formulation presents problems for the conviction of corporations - I will now turn to those issues, and suggest an alternative approach to avoid the pitfalls of the past.

Rationale and Problems: Attributing Criminal Responsibility to the Body Corporate

It has long been recognized that there is a fundamental difference between human (natural persons) and corporate defendants, resulting in problems when attributing criminal responsibility to corporations. At common law, general principles governing criminal liability are designed to prove, first, the mental element (i.e. criminal intent, or *mens rea*) and, secondly, the criminal act (*actus reus*). These concepts were developed with natural persons, not corporations, in mind.

A corporation lacks the mental characteristics attributable to a natural person, but acts through its employees, officers or agents. Traditionally, 'corporations' are considered to be legal persons which are represented through the "minds and wills' of its directors. However, in relation to safety issues in the workplace, managers, employees and officers of the corporation are usually vested with that responsibility, not the directors. So, in order to fix criminal liability on the corporation, one must look to the actions (or omissions) of those authorized by the corporation to ensure safety, and not necessarily the acts (or omissions) of the directors. This can be problematic because decision-making about workplace safety can occur in a diverse way, by a range of persons acting within the company.

Where it can be shown that a death occurred due to a corporate failure to ensure a workplace is safe, the corporation itself should be criminally liable, rather than particular employees, officers or agents of the company. There is no place for vicarious criminal liability to attach to individuals within an organization. In sentencing, the corporation itself should be the subject of denunciation and deterrence, not the managers within it. In other words, while Labor laws play an important part in discouraging practices that lead to workplace deaths and injury, the importance of the criminal law cannot be underestimated. It can denounce a corporation's conduct, or, as is often the case, the corporation's negligence (or omission to act) to ensure the safety of its workers. Furthermore, the criminal law can punish and deter the corporation (specific deterrence) involved as well as deterring other corporations from engaging in offending conduct (general deterrence).

When a corporation fails to provide for an effective system of safe work practices, and death results, it may be charged with manslaughter, i.e. where death is the result of unintentional acts or omissions. In Victoria, manslaughter can be committed by the "criminal negligence" of a corporation. "Criminal negligence" requires proof of such a gross departure by the defendant from the standard of care expected of a reasonable person as to require criminal punishment. Therefore, where a corporation has greatly fallen short of the standard of care of a reasonable person, it should be liable to be convicted of the offence of manslaughter, by criminal negligence.

For a corporation to be charged with 'manslaughter', by criminal negligence, such an offence must be included in the criminal law. In the *Criminal Code of Mongolia (Revised)* (English translation, as at July, 2014), the offence which is equivalent to manslaughter by criminal negligence is "Negligent Homicide" in Article 94. Article 94 states "Killing committed by negligence shall be punishable by imprisonment for a period of 4 years." This crime applies only to physical persons (see Article 8.1). For this offence to apply to a corporation would require three amendments to the *Criminal Code*: 1) amending Article 8.1 to apply to bodies corporate;

2) provision for the imposition of a fine, as a corporation cannot be

imprisoned; and

3) in order to distinguish civil negligence from criminal negligence, the criminal offence should be in terms of "gross negligence", that is a "gross departure from the standard of care expected of a reasonable corporation so as to attract punishment by the criminal law."

In addition, the introduction of criminal liability of corporations would require amending the *Criminal Procedure* law of Mongolia (in particular Article 5.1.6.) to redefine "parties" to include both natural persons and 'bodies corporate'.

Proving corporate criminal negligence

How is the offence of criminal negligence of a corporation to be proved? As a corporation doesn't have the 'mental state' of a natural person, traditionally, courts have reacted to this problem by adopting the 'identification principle'. That principle identifies the 'mind' of the corporation with the most proximate person to the events that caused the workplace death. That is, the identification principle of corporate liability finds proof of an act, or omission, by the most proximate natural person acting (or failing to act) with the authority of the corporation. It considers those acts (or omissions) to be attributable to the 'directing mind and will" of the corporation itself. The principle has been sated as follows: "Corporation is an abstraction. It has no mind of its own; its active and directing will must consequently be sought in the person of somebody who for some purposes may be called an agent, but who is really the *directing mind and will* of the corporation; the very ego and centre of the personality of the corporation." (*Lennards Carrying Co Ltd. v Asiatic Petroleum Co Ltd* [1915] AC 705 per Viscount Haldane). It provides for the criminal liability of a corporation only where one of its most senior officers have individually acted with the requisite fault i.e. gross negligence.

In more recent times, the leading case in common law jurisdictions on the application of the 'identification principle' is the decision of *Tesco Supermarkets Pty Ltd v Nattrass* [1972] AC 153 ("*Tesco*"). In that case, the court had to decide whether the identification principle could be applied to a store manager who was said to have been responsible for ensuring the correct prices on articles for sale. The corporation, Tesco Supermarkets P/L, was charged with a breach of the Trade Description Act 1968(UK). The issue was whether the corporation was responsible for the actions (omission) of a store manager. The House of Lords held that the store manager was not a person of sufficiently important stature within the corporate structure to be identified as the company for this purpose.

The problem with the *"Tesco"* approach is that the failure of a corporation to ensure safe work practices is more often the result of actions (or omissions) of a number of individuals within a corporation, rather than identifiable negligence of an individual, whatever their status within the company. The *Tesco* test was applied in a Victorian case, where a company and two of its employees were charged with manslaughter, and negligently causing serious injury, after a tank explosion occurred during a welding operation. One worker was killed and another seriously injured. The court (*R v A.C Hatrick Chemicals Pty Ltd* [1995] 152 A Crim R 384) held that the two managers did not embody the "guiding mind" of the company and their actions were not grossly negligent, resulting in the acquittal of the corporation. It was further held that it was unacceptable to invoke vicarious liability as the basis for a manslaughter conviction.

Both English and Australian common law continue to rely on the 'identification principle' for corporate liability for manslaughter. This is often difficult to prove where, particularly in large organizations, individuals may not have access to all the information upon which a court can base a finding of criminal negligence. In contrast, the Federal Courts in the United States of America have accepted an "aggregative model" of liability which allows the acts and mental states of individuals within a corporation to be combined to satisfy elements of the crime (see *United States v Bank of New England*, 821 F2d 844, 855 (1987)). In that case, it was found that "corporations compartmentalize knowledge, subdividing the elements of specific duties and operations into smaller components. The aggregate of those components constitutes the corporation's knowledge of a particular operation."

Due to its reliance on the identification principle, Australian courts have been unsuccessful in prosecuting corporations for manslaughter over deaths in the workplace. Statutory reforms, and proposals, have occurred in some Australian States (namely Queensland, New South Wales, South Australia, Western Australia, Tasmania and Victoria). In 2002, the Victorian Government attempted to introduce into law an offence of corporate manslaughter but the Bill was defeated in Parliament. Although it was unsuccessful, the Victorian Bill had beneficial provisions, providing a useful model for the crime of corporate manslaughter. It provided that a corporation would be guilty of "corporate manslaughter" if its conduct fell short of the standard of care that a reasonable body corporate would exercise in the circumstances and posed 'such a high risk of death or really serious injury' as to warrant criminal punishment."(Clause 14B of the *Crimes (Workplace Deaths and Serious Injuries) Bill (Vic)*, 2002). The offence of "corporate manslaughter" was defined as: "A body corporate that by negligence kills (a) an employee in the course of his or her employment by the body corporate; or (b) a worker in the course of providing services to, or relating to, the body corporate- is guilty of corporate manslaughter and liable to a fine not exceeding 50,000 penalty units (ie. A$5,000,000 or 8,600,000,000 tugrugs). Significantly, the Bill would have allowed the court to consider the conduct of the corporation as a whole, by aggregating the negligence of any number of employees, agents and officers of the corporation to determine the criminal liability of 'the corporation' (clauses 14B(4) and (5) of the *(Workplace Deaths and Serious Injuries) Bill (Vic)*, 2002). Thus, negligence by the corporation could be demonstrated by, for example, inadequate supervision and control of employees, inadequate internal systems of communication, or the failure to respond to dangerous situations of which an employee/officer/agent has actual knowledge.

The Victorian Bill therefore, required that, for a corporation to be held criminally responsible for the conduct of any of its employees, agents or functionaries, it would have to be shown that, viewed as a whole, the corporations *modus operandi*, its culture or ethos, was such as to allow a finding of criminal 'intent' sufficient to constitute criminal negligence. It did not require the actions causing a death in the workplace be due to the "guiding mind and will" of the corporation; in other words it did not require that the individual said to be responsible for the death must be in a sufficiently senior position in the corporation that he or she can be said to represent the company's "directing mind and will" (see *Tesco's case* above) at the time the death occurred. Under the provisions of the Bill, for example, evidence of corporate criminal negligence might be found in the fact that an Improvement Notice under the *Occupational Health and Safety* Act, 2004, had been served on the corporation and that the corporation had done nothing to positively redress the situation - resulting in a death which could have been avoided had the Improvement Notice been complied with.

United Kingdom legislative reform

In recent years, the United Kingdom Parliament has embarked on statutory reform, and has now created a specific 'corporate homicide' offence to replace the common law offence of manslaughter by gross negligence, for corporate offenders.

The *Corporate Manslaughter and Corporate Homicide* Act, 2007 (UK) came into force in April, 2008. It establishes a specific corporate manslaughter offence applicable only to corporations and other listed organizational types. The offence retains the "gross negligence" elements of manslaughter but seeks to relocate this negligence in the way in which an organization is managed rather than by analogy with the mind of a natural person. This formulation is likely to permit a more substantial aggregation of responsibility than previously possible in the English common law.

The offence of 'corporate manslaughter' is defined in section 1(1) of the UK Act as follows:

(1) An organization to which this section applies is guilty of an offence if the way in which its activities are managed or organized-

(a) causes a person's death, and

(b) amount to a gross breach of a relevant duty of care owed by the organization to the deceased…

The UK legislation balances the potential width of section (1) by imposing a limitation in section 1(3) – "An organization is guilty of an offence under this section only if the way in which its activities are managed or organized by its <u>senior management</u> is a substantial element in the breach referred to in subsection (1).

"Senior management" is defined to mean "the persons who play significant roles in (i) the making of decisions about haw the whole or a substantial part of its activities are to be managed or organized or (ii) the actual managing or organizing of the whole or a substantial part of those activities."

The more general focus upon senior management represents a substantial break from the restrictive 'identification principle' at common law. Despite its wider scope, the UK legislation may not be adequate to render corporations criminally liable for the acts and omissions contributing to gross negligence that occurred substantially, but not entirely, by decision-makers below 'senior management'. In that respect, it is less effective than the approach taken by the Victorian Bill discussed above.

Thus, neither attempts in Australia, nor the UK legislation, comprehensively tackle the core problems of aggregating fault at <u>all</u> layers of corporate activity. Collective organizational failure does not always occur at the levels of directors, or senior management- it may arise from the accumulation of relatively minor instances of individual negligence which combine to produce gross criminal negligence on the part of the corporation as a whole. Legal reform should include fixing liability on a corporation by allowing evidence of an aggregation of negligent acts- so the fault of the corporation may be regarded as greater than the sum of the individual acts and omissions. The individual human actors ought not be subjected to any form of vicarious liability themselves for each other's actions. The rationale for such an approach is that whilst aggregation is a totally unacceptable means of establishing criminal liability for individuals, it is uniquely appropriate for bodies corporate, which themselves are uniquely placed to ensure workplace safety, and the prevention of deaths or injury at work.

Alternative Sentences for Corporate criminal offences, including corporate manslaughter

By imposing criminal sanctions upon corporations, the court can articulate its denunciation of criminally negligent corporate conduct. Courts can also impose significant fines to deter the corporation, and others from failing to secure the workplace against dangers to its employees. Injunctive orders may be required to preserve the status quo and prevent a corporation dissolving or winding up to avoid paying a financial penalty.

Other types of penalties that may be invoked include disqualifying a company from a particular geographical area, revocation of a particular license or disqualification from tendering for particular contracts.

Adverse publicity orders should also be available as a sentencing alternative, or in addition to other penalties. Such orders would require corporations to publicize their crime and the penalty imposed. That, in itself, should act as a strong deterrent for corporations who rely heavily upon their reputation in the market place.

Community service orders may be appropriate to be imposed in some circumstances, so that the corporation can itself make amends by contributing to the wider community's safety.

Compulsory compensation orders against the corporation may also be appropriate where, for example, a death or injury has caused the victim or their family to suffer loss or damage.

And finally, the *Criminal Procedure Law* of Mongolia allows for the imposition of Orders for Costs in criminal proceedings. Pursuant to Article 99, corporations convicted of a criminal offence can be ordered to pay costs; in addition to any fine, or other sentence imposed. Unlike many 'natural person' defendants, who would not be in a position to meet any costs order, corporations should ordinarily be ordered to pay costs as part of the Sentencing Orders.

Conclusion

There is undoubtedly a need, and desirability, for corporations to be held responsible for their organizational failures which result in death or injury in their workplaces. There is a need for both procedural and substantive law reform if corporations in Mongolia are to be subjected to the criminal law for offences committed in the workplace. It is not just a matter of enhancing the Human Right to a safe workplace, but I would contend that it is also in the interests of corporations to maintain safe workplaces in order to maximize productivity.

It should not be the case that, when deaths occur in the workplace, which amount to 'corporate manslaughter' by gross negligence, that corporations are practically and legally above the law. Currently, in Mongolia, corporations are outside the jurisdiction of the criminal law. Mongolia's State Great Hural is now presented with an opportunity – it can draw on the experience of other jurisdictions to create a legal environment in which corporations can be rendered criminally liable for the aggregate criminal negligence of its employees, from its directors to its senior management down to all persons responsible for ensuring workplace safety. Subjecting corporations to the criminal law provides them with a great incentive to enhance safety in the workplace, to avoid deaths and injuries by giving higher priority to occupational health and safety.

If corporations can be charged with criminal offences arising from workplace deaths and injuries, attracting significant penalties, and public opprobrium, unnecessary deaths of Mongolians working in dangerous circumstances will be avoided; corporations will have the incentive to invest in the safety of their workers increasing work satisfaction and there fore productivity, and corporate profits. It is the refore in everyone's interests, including the corporations themselves to be vigilant to improve workplace safety practices of for all employees. It is not only a matter of international and national Human Rights, but it would prove to be an effective way of developing a culture of prevention regarding occupational health and safety in the workplace for all Mongolians.

Conclusions and Summary:

1. Too many Mongolians die (or are injured) in the workplace as a result of dangerous workplaces, where safety precautions are not followed to an adequate standard by corporate employer/ s.

2. Mongolia has international treaty obligations, national Constitutional obligations and has articulated national legal Human Rights priorities to ensure safety in the workplace for all employees.

3. Bodies corporate should be subject to the criminal law, by introducing an offence of 'corporate manslaughter" in relation to deaths in the workplace.

4. In fixing criminal liability on a corporation, the identification principle should be avoided- it too narrowly defines the range of officers/ employees in a corporation capable of contributing to corporate liability. Deaths caused by systemic failures by a corporation to establish safe systems of work should render the corporation criminally liable for the death - like any other 'unintentional homicide' committed by a natural person, when committed by a corporation acting with criminal negligence, severe sanctions should apply, together with the sigma of criminal conviction.

5. Prosecutions should be in the hands of a specialist group of procurators within the office of prosecutions, Mongolia, who work closely with the inspectors who investigate incidents under the *Labor and Hygiene* Laws, and with any specialist homicide police.

6. Prosecutions may be instituted against both domestic and international corporations which conduct business operations in Mongolia- in the fields of mining, construction and related fields, deaths should be investigated with a view to prosecuting both domestic and international corporations, if the evidence justifies it. No corporation, however large, should be immune to being prosecuted for workplace 'manslaughter' or other offences which result in death, or injury.

7. Severe sanctions should be imposed in the appropriate case, together with adverse publicity orders and costs.

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COMMODITIES FUTURES MARKET IN MONGOLIA

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Preamble

There is a Mongolian phrase meaning time does not stand still, namely, things constantly change. Because of the importance of commodities to the Mongolian economy one of the changes that Mongolians are looking forward to is the continuing development of commodities markets in Mongolia.

Introduction

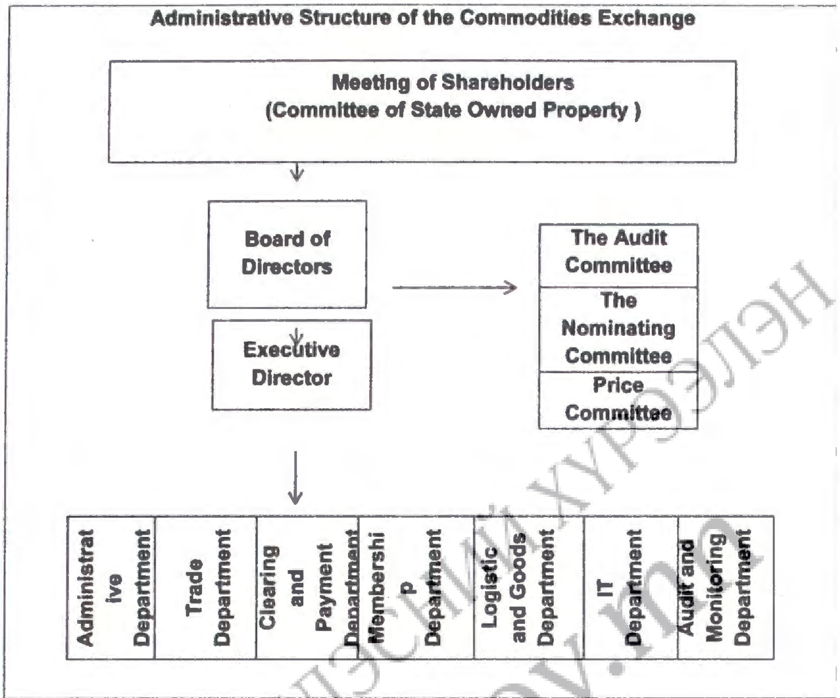
Since the 1990 democratic revolution, Mongolia has been incorporating international standards into its marketplace, for example in the securities market. While the securities exchange in Mongolia is a nascent institution, the Mongolian State Property Committee and London Stock Exchange Group have signed an exclusive strategic partnership agreement to develop and structure the Mongolia Stock Exchange. In May 2013, Mongolia revised its *Securities Market Law*, which came into force on 1st January 2014.In 2011, the Mongolian Parliament approved the *Law on Commodities Exchange of Agricultural and Raw Materials* (“***LCEARM***”) which was adopted prior to the new *Securities Market Law.*

In this *essay letter,* we will try to present basic information on the commodities markets in Mongolia on how said markets are developing.

Commodities Exchange

Whilethe Mongolian Parliament adopted the *LCEARM* in 2011, the actual history of Mongolia’s commodities exchange began on 1st March 2013 with the establishment of the Mongolian Agricultural and Raw Materials Commodities Exchange (“**Commodities Exchange**”). Pursuant to *LCEARM,* Article 7 only certain trading instruments may be sold on the Commodities Exchange, namely spot contracts, forward contracts, futures contractsand options.

Since the Commodities Exchange commencedits operations, it has only been trading spot contracts, which are defined as trading contracts for “tangible goods and raw materials.” Persons in charge of the Commodities Exchange has indicated that it is only trading spot contractsat this time because it has not yet prepared other contracts for futures, options, and forward contracts. The spot contracts traded on the exchange are done so online according to the *General Regulations of the Commodities Exchange*(“**General Regulation**”). *General Regulations* Article 7.1 states that “Payment of contracts traded on the Commodities Exchange shall be transferred by “Clearing and Payment Unit” through the banks of Mongolia, pursuant to Mongolian law”.



According to the *LCEARM*, Article 4.5 in order to be traded on the Commodities Exchange, commodities have to be approved by a member of government in charge of the related field, namely in this case the Ministry of Industry and Agriculture. As of now, the Commodities Exchange is only trading cashmere, sheep's wool, camel wool, molt wool, wheat, and oil plant(rapeseed), all of which require approval of the Ministry of Industry and Agriculture. From 3rd January 2014 to 2nd May 2014,the Commodities Exchange had sixty-one trades worth 227.3 billion Mongolian Tugrik (approximately US $12.3 million).[1] In order to participatein trading,a person or legal entity has to be a member of the Commodities Exchange, as specified in the *LCEARM*, Article 10.1.Parties may participatein commodities trading on a permanent or non-permanent membership basis. However, pursuant to the *LCEARM*, Article 10.8, foreign citizens and legal entities may only participate in commodities trading as permanent members of the Commodities Exchange. A permanent member has right to aseat, rights of trade, rights to clearing of trade but non-permanent members can only participate in the commodities trade according to *General Regulations* Article 4.3.1. On 6thMay 2014, there were thirty-five permanent members listed on the website of the Commodities Exchange[2]. Non-members of the Commodities Exchange can obviously buy or sell contracts traded on the exchange, but they cannot trade them except to a member of the exchange.

The Commodities Exchange futures market is divided into two types: hard and soft commodities. Hard commodities are typically natural resources that must be mined or extracted (gold, copper, etc.), whereas soft commodities are agricultural products or livestock products (wheat,

[1] http://mce.mn/Documents/2014.5.2pdf

[2] http://www.mce.mn/pageContents.aspx?pageID=38

wool, cashmere, etc.)[3]. In Mongolia, both types of commodities can be successfully traded as Mongolia is rich in resources and has the potentialfora large commodities market and to compete on an international scale. This is especially true of hard commodities likecoal, copper, and iron. These commodities potentially can help to create a large commodities exchange in Mongolia, even by international standards. The country's current OyuTolgoiand TavanTolgoi mining projects may form a large part of this development. The TavanTolgoi project has a"total estimated resource of 6.4 billion tons, one quarter of which is high quality coking coal. One of the world largest mine."[4]"The OyuTolgoi project promises to yield 3.3 billion tons of iron ore, 31.1 million tons of copper, 1,328 tons of gold, and 7,601 tons of silver"[5].

As stated above, Mongolia is rich in mining resources and in time those mineral resources will make their way to the domestic market place. To this end, it may be worthwhile to consider the creation of a mining commodities exchange, to coincide with the current agricultural Commodities Exchange. According to the newly-amended *Securities Market Law*, Article 3.3 the law was amended, in part, to "provide general regulations in respect of the issues and trading of derivative financial instruments, basedon goods and commodities."

Futures Contracts

The newly-amended *Securities Market Law* came into force on 1st January 2014. Some of the most important articles of which relate to the futures market.The *Securities Market Law*'s new amendments include articles regarding derivatives such as Article 19"[i]ssuing derivative financial instruments."[6] Through this article, the law provided guidelines as to who may trade derivatives, who may issue and approve derivatives,and what entity will issue the regulations that "determine the condition, requirements, and criteria to be imposed on issuers of derivative financial instruments"[7]. The newly-amended law also defined futures contracts and option contracts as follows:

Article 4.1.10 "'option contract' means a derivative financial instrument which creates for one party a right, but not anobligation, in respect of a counterparty to buy or sell a certain number of assets being the subject of the contract at an agreed price at pre-determined time and creates a corresponding obligation for the counter party"[8]; and

Article 4.1.11 "'futures contract' means a contract or derivative financial instrument that creates for relevant parties the obligation to buy or sell a certain number of assets being the subject of the contract at an agreed price at a pre-determined time."[9]

One amendment of the *Securities Market Law* that may potentially open Mongolia's futures market to international investors is found in Article 63.1.10, which states the Financial Regulatory Commission has authority to "register securities and derivative financial instruments of a domestic or foreign legal entity for public offer and for trading in the territory of Mongolia, giving permission to commence trading on the primary and secondary securities markets, suspending or invalidating trading activity for certain securities and canceling the registration of certain securities."[10] Through this article,

[3] http://www.investopedia.com/terms/c/commodities-exchange.asp

[4] www. ot.mn

[5] http://www.mongolianminingjournal.com/content/45701.shtml

[6] Securities Market Law /http://www.legalinfo.mn/law/details/9243?lawid=9243

[7] Securities Market Law /http://www.legalinfo.mn/law/details9243?lawid=9243

[8] Securities Market Law / http://www.legalinfo.mn/law/details/9243?lawid=9243/

[9] Securities Market Law / http://www.legalinfo.mn/law/details/9243?lawid=9243/

[10] Securities Market Law / http://www.legalinfo.mn/

the law provides an avenue through which foreign legal entities may enter the futures market. Prior to the passing of the law's amendments, the *LCEARM* was adopted and the Commodities Exchange had already begun trading, but only spot contracts.The Commodities Exchange is still developing, so more time is needed to prepare other types of contracts, such as futures and options. However, in order to trade futures contracts, the Commodities Exchange would need to have a standardized contract. The authority to create a standard contract forfutures trading is vested in the Financial Regulatory Commission and the relevant securities trading organizations via the new *Securities Law*,Article 19.3.[11] Thus, it is the responsibility of organizations like the Financial Regulatory Commission to prepare standardized contracts for use of commodities already registered on the Commodities Exchange, since only standardized contracts can be traded.

Commodities Being Traded

Some developed countries have awell-developed futures market, like the Singapore Commodities Exchange, the Chicago Mercantile Exchange Group ("CME Group"), and the EurasianTrade System Commodities Exchange of the Republic of Kazakhstan. All of these exchange strade both soft and hard commodities via futures contracts. This arguably strengthens these institutions and provides an environment for increased development. For example,the CME Group has ten different categories for exchanges, which are agriculture, energy, weather, metals, options, real estate, interest rates, and an equity index.[12] All categories are regulated by one institute, the commodities exchange.

In Mongolia, there is only one Commodities Exchange, which trades agricultural commodities pursuant to the*LCEARM*. Compared to other international commodities exchanges, the Mongolian Commodities Exchange is a new exchange, created only in 2011. According to the *LCEARM*, Article 4.6, in order to export commodities that are approved to trade at Commodities Exchange,they must be traded on the Commodities Exchange. In addition, the *LCEARM*, Article 4.7 provides that a bonus should be given to partners, agricultural industry persons, and legal entities, if their commodities are traded on the Commodities Exchange.[13] These kinds of inducements can be found in other developing countries' legislation as they are beneficial to farmers.

Currently Mongolia is only trading soft commodities; in order to trade hard commodities like metals, the *LCEARM* must be amended, since pursuant to the *Securities Law*, Article 3.3 it requires promulgation of general regulations with regard to the issue of trading commodities. Detailed regulationsare to be provided in specific laws and regulations[14].

Conclusion

The futures market was a new concept in Mongolia until 2011, just as the commodities futures market was a novel idea until the early eighteenth century in the United States of America. Currently, the development of the commodities futures market is now underway in Mongolia.The Commodities Exchange of Mongolia is aiming to organize its first futures contract trading in 2014,

law/details/9243?lawid=9243/

[11] *SecuritiesLaw* article 19.3 The relevant securities trading organization and the FRC shall determine the conditions, requirements and criteria to be imposed on issuers of derivative financial instruments, the standards applicable to derivative financial instruments and the procedures for trading the same.

[12] http://www.cmegroup.com/

[13] http://www.legalinfo.mn/law/details/567?lawid=567

[14] Securities Law, http://www.legalinfo.mn/law/details/9243?lawid=9243

according to the Exchange's official web page. The first objective to begin trading commodities futures is to draft a standard futures contract and specific rules for futures trading. These documents are already in the process of finalization, but the first draft is not yet available to the public. The Commodities Exchange is definitely taking the first big step towards development of Mongolia's futures market and the Commodities Exchange will bekey in this development. It has been three years since Mongolian Parliament adopted the *LCEARM* and revised the *Securities Law;* and the Commodities Exchange is trying to accelerate the development of the commodities market in Mongolia. With natural resources like coal, copper, molybdenum, iron, uranium, and gold, the Commodities Exchange can be a very busy organization.

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