

Legal summary of the Corporate governance code of Mongolia

The issue of a corporate governance started to receive attention in Mongolia since the year 2000, and it is viewed that development of corporate governance in our country is important for creation of appropriate conditions for sustainable and proper management and organisation of companies, in particularly of publicly listed companies, so that trust bonds between shareholders and companies is maintained and ability of companies to attract investment is improved.

Therefore, the Corporate Governance Code of Mongolia has been developed by taking into account internationally recognised OECD principles of corporate governance, recommendations proposed by ADB, EBRD and other international organisations, international best practices and experiences, and local specific conditions and realities.

The code is structured into 10 chapters, and content wise comprises guidance, recommendations and explanations in addition to main principles to be pursued.

Corporate governance principles: The principles of corporate governance included in this chapter serve as the grounds for identifying the fundamental principles for management of business operations of the company, and should be based on principles of respecting rights and lawful interests of stakeholders. In particular, they should comply with lawful interests of stakeholders such as increasing capital of companies, creating jobs, securing the financial stability and improving profitability. These conditions are formed by appropriate corporate governance principles as follows:

1. Corporate governance should provide genuine possibilities to shareholders to exercise their rights.
2. Corporate governance should guarantee the principle of equal treatment for shareholders of a same class. In case of violation of rights, shareholders shall have the opportunity for redress.
3. Corporate governance should provide the company activities with strategic management and confer to the Board of Directors the possibilities of effectively supervising the activities of executive management and reporting to the shareholders.
4. Corporate governance should guarantee opportunity for the executive management to conduct its activities properly and honestly in accordance with interests of the company and the executive management should report its tasks to the Board of Directors and shareholders of the company.
5. Corporate governance should ensure an environment where shareholders and investors may obtain correct and complete information required for producing a reasonable decision on a timely basis regarding the company's financial situation, economic indicators and ownership and management structure.
6. Corporate governance should consider the rights specified in the law of stakeholders such as employees of or creditors to the company from the viewpoint of increasing the value of corporate capital, shares and other securities and creating more job vacancies.

7. Corporate governance should establish a system to impose supervision on corporate activities for the purposes of protecting interests and lawful rights of shareholders and stakeholders.

Meetings of shareholders: A person owning shares of the company assumes risks by his/her invested capital, therefore, should receive specific and complete information from the Board of Directors and the executive management regarding their policies. Meetings of shareholders provide an opportunity for them to participate in company activities, reduce investment risks, to increase the level of dividends as a reward of investment. Therefore, organising meetings of shareholders in a proper manner and present a possibility for shareholders influence policies and strategies by casting vote on major decisions regarding company activities and to receive accurate and full information.

Call for the shareholder meeting and holding the meeting of shareholders is mainly regulated in this chapter as meetings of shareholders present an only possibility for minority shareholders to obtain information regarding company activities and to raise questions on issues related to the management of the company.

Board of the directors: The Board of Directors is primarily in charge of defining strategic policy and imposing oversight on activities of the executive management and managers of the company. Company should develop, get approved by the Board of Directors and enforce “Operational Rules for Board of Directors” covering nomination criteria for members of the Board, selection process, re-election conditions, criteria for independence, operational rules for Board and its committees, announcement of the general shareholders meeting, procedures for participating in meetings, information dissemination to members, sanctions imposed for members who failed to fulfill their functions, compensation policy.

This code expanded the provisions related to the responsibilities and the functions of the Board of directors, for example, the article 3.1.4 provides that the Board of Directors should protect legitimate interests of shareholders. This shall be achieved by the following:

1. The Board of Directors should employ an officer in charge delivery of information about company activities and other material information, a procedure should be set in place for information disclosure, and monitoring of enforcement should be exercised.
2. The Board of Directors shall establish regulations to prevent and deal with conflict of interest between shareholders and corporate units, or among shareholders.
3. The Board of Directors shall exercise control over disclosure of information by the executive management to the shareholders.

Executive management: The role of executive management is to provide management in running daily activities of the company in compliance with the business plan, ensure implementation of decision issued by the Board of Directors, its committees and supervisory council, respect legitimate rights of shareholders, increase profitability of corporations, and thus return on investment for shareholders. Principles and recommendations included in this chapter

are significant for exercising above roles and for building understanding and trust among investors, shareholders, and corporation. Following aspects enacted in this section of the code:

1. Powers of executive management;
2. Composition of the executive management; and
3. Duties, responsibilities and incentives of executive management.

Disclosure of information and transparency: The timely disclosures of relevant information by the company will increase the confidence of shareholders and stakeholders and prevent unfair use of insider or classified information. Companies should develop procedures to regulate disclosure of information as specified by the law, regulatory bodies, and other material information, and the Board of Directors is responsible for approval and enforcement. Under article of the code, following information should be disclosed:

1. Information about Board members, key executives and adopted changes;
2. Information on independent directors of the Board;
3. Owners of more than 5% of total shares issued, people and legal entities representing common interests /if those own company shares/;
4. Information if owners of more than 5% have changed; or
5. Large borrowers, customers etc.

Stakeholders: Business partners such as banks, financial institutions, other creditors, insurers, suppliers, contractors, clients, customers, employees, their representative bodies, regulatory bodies should be considered as company stakeholders. Rights of the stakeholders specified in law and provisions of the contract should be protected. The company and stakeholders should cooperate on the basis of the mutual benefit. Following aspects enacted in this section of the code:

1. Protection of rights of stakeholders; and
2. Monitoring by stakeholders of company activities.

Financial and accounting auditing system: Auditing system intends to improve confidence of investor about the company and its management. Its purpose is to ensure invested funds and company assets. Company's internal auditing system should be divided into supervisory council which is appointed from and reports to the shareholders meeting. Auditing committee which is comprised of Board members and internal supervision unit to operate under executive management, and the term independent auditing system means professional auditing firms, auditors which perform independently from the company.

In the company legislation, it is provided to have to bodies to control corporate activities, supervisory council and independent audit. Those are supposed to exercise control and monitoring of financial and economic activities of the company once a year, verify accuracy of financial reports, therefore they have limited opportunity to monitor activities on a daily basis.

Dividends: Dividend allocation, distribution mechanisms should be clear. To this end, dividend policy should be approved and enforced by the Board of Directors. Evaluation of companies by shareholders directly relates to dividend policy. It is expected to gain some earnings when

investment decision is made and company shares are bought. Therefore, current and future shareholders should have a clear understanding about dividend policy, minimum level of dividend allocation, form of dividend payout. The code provided that these issues should be covered in dividend policy paper developed by the Board of Directors. Board of Directors should publicly disclose dividend policy. Secretary of the Board also should ensure that this document is available to all interested people and publish it on the company website.

Regulation of conflicts of interests: Possibility to prevent and regulate conflicts of interests shall protect rights of shareholders, property and reputation of the company. Effective mechanisms to prevent conflicts of interests or regulate the occurring ones is crucial to resolve the before initiating and to assist the parties investigating the conflict of interests to settle the matter. Company management shall take actions to resolve conflict of interest that might arise related to areas under their authority. Under article 9.5 of this code, in order to realistically evaluate the conflicts of interests, it is essential to establish an effective regulation to settle such conflict without involving the conflicted parties or parties with a potential to conflict.

Summary

This Code was developed to be used specifically by publicly traded companies, i.e. joint stock companies, and can also be used by limited liability companies and other legal persons upon making certain adjustments to suit own special features. Each company in Mongolia will introduce and implement corporate governance principles in their daily operations, furthermore, create sustainable corporate development and favorable investment conditions and make significant contribution in the rapid economic growth.

This summary is informative and of a general nature. We recommend that no one should act on the basis of such information without appropriate professional advice after a thorough examination of the particular situation.

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