Case study
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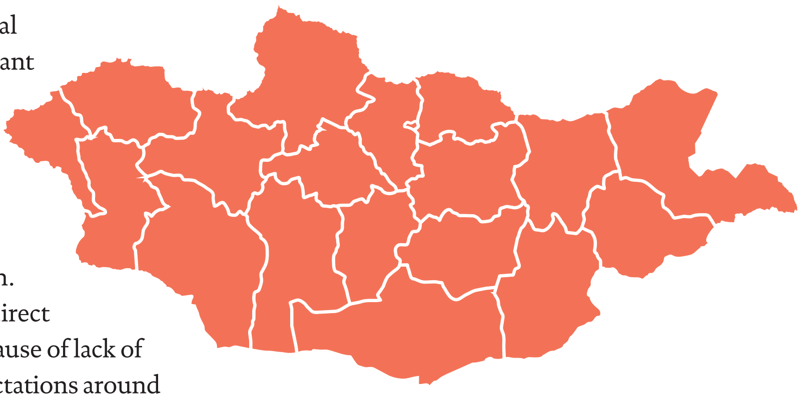
Natural Resource Governance Institute

Mongolia Revenue Sharing



Nicknamed "Minegolia" for its enormous natural resource potential, Mongolia is already a significant copper, gold, and coal producer and a small producer of oil and gas. In a country where local communities are often very small, scattered andimpoverished, and there is a general lack of infrastructure or social services, expectations from large mining projects are high. Mining communities often find themselves in direct conflict with companies or the government because of lack of regulations or dialog, as well as unrealistic expectations around resource-related benefits.

Over the last few years, the country has witnessed increasingly frequent conflicts between affected communities and mining companies. For example, in recent years local community representatives confronted companies for environmental, local content, transparency and economic issues in almost all major mining regions. These include Huvsgul over the impact of phosphorus deposit development, Umnugovi over the water issues on Rio Tinto's Oyu Tolgoi project, and Dornogovi over the impact of uranium exploration on livestock and human health.

Mongolia is a unitary state with a degree of political and fiscal decentralization. Aimags (provinces) are governed by an elected local parliament. Governors are approved by the Prime Minister. The local parliament can set its own legislation which cannot be overruled by central government institutions if it does not breach the law. Most aimags have Citizens' Halls, which are used to discuss spending proposals by the government before actual decisions are made. Residents and other relevant stakeholders directly participate in the process. Soums (sub-provinces) are accountable to the aimags. The expenditure responsibilities of each level of government are presented in the table below.

Most government revenues from the mineral and oil sectors are centralized. While aimags have no tax collection authority, the capital city and soums can collect small fees and a few ancillary taxes (see table below). Aimags and soums cannot sell mineral licenses, however they are consulted during the licensing process and are allowed to sign community development agreements with companies.

Some mining-related revenues are distributed to local governments through earmarking and local development funds. Twenty five percent of domestic VAT payments, 5 percent of mining royalties, 30 percent of petroleum royalties, and budget surpluses of local governments are distributed to local governments. These funds are collected into the General Local Development Fund then redistributed to aimags and the capital city according to a formula that includes population, population density, remoteness, size of the territory, development indicators and tax generating capacity. Then, aimags and the capital city redistribute at least 60 percent of the fund to the lower level soums or horoo in case of the capital city.

Recently, local governments in mining regions have complained that they are not receiving large enough compensation compared to the non-mining regions because of the costs associated with mining at the local level. To voice their concerns, local governments supported only 6 percent of mining applications in the first quarter of 2015.

In response, the government passed a new law whereby 65 percent of mining royalties will go to the central government, 5 percent will continue going to the General Local Development Fund and then redistributed according to the formula, and 30 percent will go directly to mining aimags, of which one third is reallocated to the soums. What's more, 50 percent of license fees will go directly to the mining aimag's local development fund, of which 50 percent is sent to the soums. This law, which only applies to certain mining projects, will go into effect in 2016.

Expenditure responsibilities by level of government

National	Capital city and aimag	Soum
• Education services • Health services • Defense • Pensions • Foreign affairs • Mining • Energy • Industrial policy • National transport infrastructure (e.g., roads, railways)	• Urban planning and establishing new infrastructure • Social care, welfare services and poverty alleviation • Development of small and medium-sized enterprises • Water supply, sewerage and drainage systems • Housing • Public transport • Environmental protection and rehabilitation • Large scale roads and bridges • Utilities for public areas, landscaping, public hygiene, street lighting, cleaning, and waste removal • Maintaining electrical infrastructure	• Utilities for public areas, public hygiene, street lighting, cleaning and waste removal • Protection of nature and the environment • Public lighting • Maintenance of sidewalks, recreational areas and children's playgrounds

Revenues by level of government

National	Capital city and aimag
• Corporate income tax • Value added tax • Excise tax • Customs duties • Fuel and diesel tax • Mineral royalties • Mining license fees • Air pollution fees • Water pollution fees • SOE dividends	• Personal income tax • Land use fees • Immovable property tax • Vehicle tax • Water use fee • Common minerals royalty • Income on local property