[Symbol of Mongolia]

ERDENECHIMEG LUVSAN
MEMBER OF THE STATE GREAT HURAL OF MONGOLIA

State Palace, Great Chinggis Khaan Square 1,
Sukhbaatar district, 14201 Ulaanbaatar city
Tel: 26-05-55, Fax: 32-70-16
E-mail: erdenechimeg@parliament.mn
http//www.parliament.mn

Date: 2 July 2015 Ref. number: 4/6299

TO MR. ENKHBOLD ZANDAAKHUU,

THE SPEAKER OF THE STATE GREAT HURAL OF MONGOLIA

Re: Submission of a Conclusion

I hereby submit the conclusion of the Working group established by the Ordinance No. 101 of 2015 of the Speaker of the State Great Hural.

Please grant us the permission to distribute the conclusion to the members of the State Great Hural.

Sincerely,

MEMBER OF THE STATE GREAT HURAL /signed and sealed/

L. ERDENECHIMEG

STATE GREAT HURAL'S (THE PARLIAMENT)

WORKING GROUP CONCLUSION

22 June 2015

The Speaker of the State Great Hural (the "Parliament") established a working group (the "Working Group") by his order with number 101 of 2015. In accordance with the guidelines [of the Speaker], the Working Group has reviewed the "Cooperation Agreement", "Investment Agreement", "Agreement for Construction-Ownership-Operation-Transfer of Railway Base Structure for the Route of Ukhaa Khudag-Gashuun Sukhait" which are proposed to be concluded with the Consortium who will operate Tavantolgoi Coal Deposit (which were submitted to the Parliament on April 23 [2015]) as well as other necessary matters related thereto and hereby submit this conclusion and a draft decision.

During the preparation of this conclusion, we made various enquiries to and obtained information from related Government organizations and companies in relation to necessary issues. (*Copies of related enquiry and information are attached*)

In addition, the Democratic Party group in the Parliament and 16 members of the Parliament who are led by MP L.Erdenechimeg received answers from M.Enkhsaikhan, the Minister of Mongolia in response to their enquiries about the Investment Agreement and other related agreements to be concluded with the Consortium which will operate the Tavantolgoi Coal Deposit. We have taken the answers of Minister M.Enkhsaikhan to such enquiries as a source of this conclusion since those answers are considered as official evidence. (*Enquiry from the Democratic Party group in the Parliament and enquiry from the Parliament Members led by L.Erdenechimeg are attached together with the respective answers of Minister M.Enkhsaikha*n)

"Energy Resources" LLC is defined as "Project Company" in the second part of the definition of "Parties" in the Cooperation Agreement and in the fifth part of definition of "Parties" in the Investment Agreement.. Therefore, in this conclusion, we hereinafter refer to the term "Project Company" as "Energy Resources" LLC (in short "ER").

Introduction

A brief review of Erdenes Tavan Tolgoi JSC's operations in mining

Erdenes Tavan Tolgoi JSC was established in 2010, and took the licenses from Erdenes MGL to operate mining activity. Erdenes Tavan Tolgoi commenced mining operations at the East Tsankhi Block and West Tsankhi Block, respectively, on 27 August 2010 and 16 February 2013.

The deposit is situated 540 km south of Ulaanbaatar, 90 km east of Dalanzadgad city, the capital of Umnugobi province, 16 km southwest of Tsogttsetsii sum and covering an area of 220 square km.

Erdenes Tavan Tolgoi JSC owns the following mining licenses MV-011943 (2,046.4 hectares), MV-016883 (700.39 hectares), MV-016881 (556.72 hectares), MV-

016882 (2,447.13 hectares), MV-011953 (12,864.47 hectares), MV-011954 (22,901.37 hectares), MV-011955 (28,813.1 hectares), MV-011956 (3,151.92 hectares) that covers 68481.5 hectares.

The Tavantolgoi coalfield consists of six coalfields: Tsankhi, Ukhaakhudag, Borteeg, Onchkharaat, Oortsog, Bortolgoi, from which Tsankhi is the only coalfield that detailed studies were conducted for operation.

Coal Reserve:

Tavantolgoi coalfield estimated to contain a total of approximately 7.4 billion tons of JORC coal resources comprising 985.5 million tons in measured category, 2,986 million tons in indicated category and 3,410.6 million tons in inferred category. This includes 5.4 billion tons that are classified as coking coal and 1,9 billion tons that are classified as thermal coal.

- Coal bearing unit Tavantolgoi from Tavantolgoi coalfield has sixteen named coal seams (Seam 0 through 15). Seams have a thickness of 1-82.5 meters.
- In Tsankhi area indicated ten coal seams (Seam 0 through 9)
- Commercial six coking and semi coking coal seams are Seam 0, III, $IV^{АБВ}$, $IV^{АБВ}$, $IX^{АБВГ}$

Feasibility Study

Norwest has completed a feasibility study for development of East Tsankhi mine area in 2009, Prefeasibility study for West Tsankhi Mine area in 2011.

A feasibility study for development of East Tsankhi mine area was prepared by Absolut Mining in April 2011 and a feasibility study for development of West Tsankhi mine area was prepared by Mining Institute in June 2012. Both feasibility studies are approved by Mongolian Mineral Resources Counsel.

Technical and Economic Indicators for development of East Tsankhi's Open Pit

- Coal Reserve /A+B+C/-750.47 million ton
- Annual production capacity- 15 million ton/year
- Average annual soil stripping (overburden) volume-43,5 million m^3
- Coal Handling and Preparation Plant (15 million ton /year)

Mining production will reach its full capacity from fifth year as reflected in the project plan. It is projected to extract from Seam IV in the initial 3 years and seam 0, III from 4^{th} year forward.

Technical and Economic Indicators for development of West Tsankhi's Open Pit.

- Coal reserve/A+B+C/-814,1 million ton
- Annual production capacity-15 million ton/year

- Average annual soil stripping volume-55 million m^3

It is projected to extract from Seam IV in the initial 3 years and seam 0, III from 4 th year forward.

East Tsankhi mine

Mine's soil stripping started in August 2010 and from the 2011 Macmahon, Australian company, is working as an operator. The indicators during the operation: sub-corner's height is 4 meters, main corner's height is 12 meters, decline's degree is 55. As of 2014, area of A and B mines are 130 hectares, the deepest hole will be 85 meters. There are 3 main exits/sewages, soil and coal are located 2-2.5 km and 0.5-1.5 km away from the mine respectively.

In 2010 545,000 m^3 soil, in 2011 0.9 million ton coal and 3.8 million m^3 soil, in 2012 2.5 million ton coal and 8.5 million soil, in 2013 2.7 million ton coal production and 9.2 million m^3 soil stripping has been done. As of 2014, 0.9 million ton coal have been produced and 4.6 million m^3 BCM work have been done. Australian company, TTJVCO Ltd, is working as an operator and stopped operation since 14 August of 2014 to make negotiations and agreement better.

The negotiation resulted mainly in reducing the cost of production by 50%, making the payment relevant to the performance of the production. The parties are working on to begin the production as soon as possible.

There are 8 excavators that have capacity of 5-36 m^3, 20 dump trucks that have capacity of 55-240 tons used in mine. When the coal price start to raise, the current production capacity could be increased to 15 million ton per year.

Indicator	2010	2011		2012		2013		2014		2015	
	Performance	Feasibility Study	Performance	Feasibility Study	Performance	Feasibility Study	Performance	Feasibility Study	Performance	Feasibility Study	Performance
Coal production million ton	-	1.0	0.9	3.0	2.5	6.0	2.7	10.0	0.9	15.0	-
Soil stripping million ton	0.5	3.3	3.8	10.3	8.5	20.6	9.2	43.0	4.0	48.0	-
BCM million ton	0.5	4.0	4.4	12.4	10.3	24.9	11.2	50.1	4.6	59.5	-
Stripping ratio m3/ton	-	3.3	4.2	3.4	3.4	3.4	3.4	4.3	4.4	3.2	-

West Tsankhi mine

The operation started in February 2013 and the "Mongolian Miners" partnership works as an operator. Transportation and outside dumping system used on the mine site. There are 3 main exits/sewages, which 2 of them are soil exits and 1 is used for coal transportation. Soil and coal are located 1.2 km and 1 km away from the mine respectively.

The indicators during the operation: sub-corner's height is 4 meters, main corner's height is 12 meters, decline's degree is 55. As of 2014, the operation covers 130 hectares, the deepest hole will be 60 meters.

In 2010 545,000m^3 soil, in 2011 0.9 million ton coal and 3.8 million m^3 soil, in 2012 2.5 million ton coal and 8.5 million soil, in 2013 2.7 million ton coal production and 9.2 million m^3 soil stripping has been done. As of 2014, 0.9 million ton coal have been produced and 4.6 million m3 BCM work have been done. Australian company, TTJVCO Ltd, is working as an operator and stopped operation since 14 August of 2014 to make negotiations and agreement better.

There are 13 excavators that have capacity of 5-17 m^3, 57 dump trucks that have capacity of 55-130 tons used in mine. 2-3 million m^3 BCM work is done monthly.

By 1st quarter of 2014, from West and East Tsankhi 139,800 ton coal produced and 774,200 ton exported compare to the 1st quarter of 1,439,600 ton has been produced and 1,819,400 ton coal been exported.

One. Whether the Cooperation Agreement, the Investment Agreement, and the Railway Concession Agreement in relation to the operation of which are the Tavantgolgoi Deposit that are submitted by the Government, comply with current legislation

1.1 The Cooperation Agreement

The draft Cooperation Agreement (hereinafter "Agreement") was prepared for the purpose of operating the Tavantolgoi Coal Deposit, to be concluded by and among (1) "Erdenes Tavan Tolgoi" JSC (hereinafter "ETT"), a Mongolian state owned joint-stock company, (2) "Energy Resource Corporation", 100 percent subsidiary of "Mongolian Coal Corporation" of Luxembourg, (3) "Energy Resource" LLC (hereinafter "ER"), 100 percent subsidiary of "Energy Resource Corporation", and (4) "China Shenhua Energy Company Limited" (hereinafter "Shenhua").

As stated in Article 4 of the Cooperation Agreement, "Energy Resource Corporation" and "China Shenhua Energy Company Limited" are the investors of ER.

1.1.1 Under the part D of the Recitals and Articles 1.1 (a), 1.2 (b), and 6.1 (d) of the Agreement, ETT transfers all of its rights and some specific obligations related to the mining operation under its mining license for Tsankhi mine area as well

as its land possession right to ER for the total Term of the Agreement (main Term for both of the Cooperation Agreement and the Investment Agreement is 30 years respectively and extension Term is 30 years respectively).

The mining license of ETT is not assignable or transferable to ER, therefore, ETT, the mining license holder, must keep[1] its rights and obligations under its mining license according to the Mining Law.

Therefore, the abovementioned provisions of the Cooperation Agreement about the assignment of the rights and obligations violate Articles of the Minerals Law related to rights and obligations of mining license holder in its entirety.

1.1.2 Under Article 1.2 (a) of the Cooperation Agreement, ETT is transferring its land possession right to ER free of charge for the Term of the Agreement. Furthermore, under Article 5.1 (j) of the Cooperation Agreement and Article 5.7 (a) of the Investment Agreement, ER has the right to obtain land use or possession right which is required to perform other operations of the Project and through its related organizations, the Government shall grant the land use or possession right to ER and its Affiliates.

The act of ER receiving or obtaining the **land possession right** for the Tavantolgoi violates Article 6.3 of the Land Law which states that "Foreign countries, international organizations, foreign legal entities, legal entities with **foreign investment**, foreign citizens and stateless persons may become a land user for a specific purpose, duration, terms and conditions and on the basis of a contract in accordance with law".

Part (H) of the Recitals of the Investment Agreement provides that "China Shenhua Overseas Development and Investment Limited" and domestic investors shall, directly and indirectly, own Energy Resources LLC ("ER") which now operates Ukhaa Khudag Deposit by establishing a joint venture.

Therefore, ER will be reorganized as a legal entity with foreign investment which is invested by ERC (Energy Resources Corporation) of Luxembourg and Shenhua of China, and as such it cannot hold a land possession right according to Article 6.3 of the Land Law.

Furthermore, if ER's affiliated companies which will carry out activities stated in Article 5.7 (a) of the Investment Agreement are foreign invested entities, then they will not also be able to hold any land possession rights.

1.1.3 Under Part E of Recitals and Article 5.1 (q) of the Cooperation Agreement, ETT is transferring its certain liabilities and **assets** including existing employees working for Tsankhi mine area, contracts for sale of coal from Tsankhi mine area and contracts for provision of mining services, and other agreements to ER by concluding a separate "Transfer and Novation Agreement".

[1] Translation note: "keep" - must not assign or transfer

Transferring the assets of ETT, which is a state owned company, to ER will trigger **privatization** issue. **Therefore, the aforesaid provisions breach Article 29.1 of the Law of Mongolia on State and Local Property which states that "In the event when the state owned immovable properties are being sold by means other than privatization, the auction procedure must be followed by decision of the Government, whereas for the sale of movable assets that are in the fixed assets of State owned entities, the auction procedure must be followed by the decision of the State Property Committee, and for other assets the auction procedure must also be followed by the decision of the relevant legal entity, respectively."**.

Furthermore, the transfer of assets, certain liabilities, and employees of ETT to another company must be decided according to Article 87 (Major Transactions) of the Company Law.

However, it appears that the negotiation to enter into Cooperation Agreement and the Investment Agreement were conducted prior to ETT making its decision pursuant to Article 87 (Major Transactions) of the Company Law. Article 87 of the Company Law will be breached in its entirety if the "Transfer and Novation Agreement" is entered before such decision is made.

1.1.4 Article 6.1 (i) of the Cooperation Agreement provides that ER shall have the right to own the coal extracted from Tsankhi mine area.

Article 6.2 of the Constitution of Mongolia states that "the subsoil and its wealth shall be the property of the State" and Article 5.1 of Minerals Law further clarifies this provision by stating that "Mineral resources naturally occurring on the land surface and subsoil of Mongolia are the property of the State".

Moreover, Article 5.2 of the Minerals Law states that "the State, as the owner, has the exclusive authority to grant the right for prospect, exploration and **use (i.e., mining) of** minerals according to the terms and conditions set forth in this law". Accordingly, ETT, a State owned entity, has the right to use (i.e., mine) Tsankhi mine area of Tavantolgoi as the holder of the mining license. Based on the provisions of the Minerals Law, the State does not have the right to transfer the minerals ownership rights but it can only grant the right to use or mine minerals through licensing.

Therefore, ER does not have the right to own coal mined from Tsankhi mine area. Nevertheless, Article 29.4 of Investment Agreement provides that "ER shall be an independent contractor ... under this Agreement".

1.1.5 Article 5.1 (k) of the Cooperation Agreement states that ER will obtain all documents listed in Article 35.3 of the Minerals Law. This clause conflicts with Article 35.3 of the Minerals Law which stipulates that all those documents must be kept by mining license holder which is ETT.

1.1.6 Article 5.1 (o) of the Cooperation Agreement provides that "in order to exercise the rights and obligations of the holder of Tsankhi Mining License, **ER** shall have the right to lodge any request, complaint or claim to the respective state organizations, authorities, courts, officials **without obtaining any power of attorney from ETT**".

It breaches the relationship that must be established on the basis of a power of attorney specified in Chapter 7 "Representation" of the Civil Code in its entirety.

Moreover, the provision that states "ER has the right to file a complaint or claim to courts without power of attorney issued by ETT" violates Article 35.2 of the Civil Procedure Code which states that "A person who is representing a legal entity must present to the Court a document certifying his/her official position or authority to act as a representative on behalf of such legal entity" and Article 36.2 of the same law which states that "Full authority of a representative shall be determined by the power of attorney and other written authorization documents issued by an appointing person. The power of attorney may exclude some of the rights afforded to the participants of a legal proceeding in the adjudication process. The power of attorney must meet the requirements prescribed in Article 64.2 of the Civil Code".

1.1.7 **Under Article 13 of the Cooperation Agreement**, **ER obtains and maintains the right to prepare and execute documents and to deliver to the relevant organizations, to take all types of actions required to carry out the mining operations on behalf of or as a substitute for ETT.**

This provision limits ETT's legal rights to correspond to other organizations. Since ETT has not transferred its mining license to ER, it must, by itself, perform its rights and obligations related to the mining license in accordance with the Minerals Law and be responsible for it before the relevant authorities.

Obtaining and maintaining aforesaid rights by ER is equivalent to indirect transferring of the ETT's mining license to ER.

Upon conclusion of this Cooperation Agreement, ETT will not be liquidated but it will keep its legal capacity. Therefore, it is not necessary for ETT to grant a right to ER to substitute ETT and to take all necessary actions on behalf of ETT.

1.1.8 As stated in Article 6.1 (j) of the Cooperation Agreement, ETT has the obligation to **unconditionally and promptly** provide ER with all necessary administrative and technical supports and cooperation including but not limited to any approval, permit, signature, chop (or stamp), authorization, power of attorney, documents, information and other cooperation.

Under this provision, ER is making ETT incapable of exercising its corporate governance and management. Furthermore, this provision is unacceptable for that it infringes the ETT's legal rights granted by the Company Law and the Minerals Law. Specifically, the unconditional obligation is too one-sided and conflicts with the business principle of equality and mutual cooperation.

1.1.9 As stated in Article 8.1 (b) of the Cooperation Agreement, ER and the Investors have the right to charge or assign by way of security its **rights, interest, benefit under this Agreement in favor of the Investors or Financiers for the purpose of raising financing**.

This provision is the most controversial and unacceptable clause for the Government and ETT.

According to Part D of the Recitals and Articles 1.1 (a) and (b), 1.2 (a), and 6.1 (d) of the Cooperation Agreement, ETT is assigning and **transferring** all of its rights and some specific obligations related to the mining operation under its mining license for Tsankhi mine area as well as its land possession right to ER for the total Term of the Agreement (initial Term for both of the Cooperation Agreement and the Investment Agreement being 30 years respectively with 30 more years of extension each).

In addition, under Articles 5.1 (e) and 6.1 (i) of the Cooperation Agreement, ER has the ownership rights and title over the coals extracted and processed (washed) from the Tsankhi mine area. ER has the right to transfer, by way of creating security, these rights and interests (First) to the Investors and (Second) to the Financiers.

Under this Agreement, the Investors are “Energy Resource Corporation” which is 100 percent owned subsidiary of “Mongolian Coal Corporation”, a Luxembourg company and “China Shenhua Energy company limited” which is a Chinese state owned company.

In Article 30.1 (g) of the Investment Agreement, the term “Financier” is defined as any international investor or banking and financial institutions including but not limited to export credit agencies, development banks, commercial banks of PRC and Japan, and multilateral financial institutions which provide loans to ER.

From these provisions related to pledge, we conclude that ER intends to create security and pre-planned to transfer Tavantolgoi coal deposit by this method (by creating security over it). In other words, it leads to the conclusion that ER intends or plans to transfer its rights, interests and benefits under this Agreement to a third party by creating security over them with eventual transfer. Because, ER is owned by MMC, a company registered in the Cayman Islands, through its subsidiaries in countries such as Hong Kong, Luxembourg, and Mongolia; and as of 3 May 2015, MMC had a debt of USD570 million owed to international banking and financial organizations and USD600 million in the form of bond. The total debt of this company is USD 1 billion and 170 million. As a security for these debts, ER pledged or created security over its coal washing plant, power plant, assets, cash, and shares of its subsidiary companies “Mongolian Coal Corporation” in Hong Kong, and “Mongolian Coal Corporation” S.A.R.L in Luxembourg. (*Detailed conclusion is provided in the part 14.7 of this paper under Right of pledge*)

However, Article 8.2 (b) of the Cooperation Agreement prohibits ETT, the legal holder of mining license for Tavantolgoi deposit, from creating any security and this provision conflicts with Article 51.1 of the Minerals Law under which ETT has the right to pledge its licenses to a bank or non-banking financial organization for the purposes specified in the law or to finance the operations of the deposit.

1.1.10 Under Article 8.2 (c) of the Cooperation Agreement, ER has the preemptive right to obtain the ETT mining license by transfer in that the event ETT decides to sell, transfer or otherwise dispose of the Tsankhi Mining Licenses.

This provision of the Agreement conflicts with Articles 49.1 and 49.3 of the Minerals Law. According to these articles of the law, the license holder, ETT, may

transfer its license to a newly established entity which takes over its rights and obligations as a result of a merger and acquisition; or to its parent company, or to an entity which purchased its mine.

Furthermore, this provision conflicts with Section 1.a of the Government Resolution number 268 of 2014 with respect to "Some measures to take concerning the Tavantolgoi Deposit" which states that "[Tavantolgoi deposit] shall be used under "Investment and Cooperation Agreement" without transferring the mining license for Tavantolgoi deposit held by Erdenes-Tavantolgoi, a State owned entity".

The non-transferability of the mining license is the main condition for the cooperation with investors. Therefore, this provision should not be included in the Cooperation Agreement and the main requirement of the competitive bidding[2] will be violated if the mining license is transferred to ER in any manner.

1.1.11 Article 8.2 (d) and (v) of the Cooperation Agreement restricts the legal rights of ETT by stating that "the Tsankhi mining license shall **be transferred in its entirety [as a single license covering all the licensed area] and shall not be transferred in parts**".

The Tsankhi has two parts: east and west and the aforesaid provision prohibits ETT to manage them within its authority in connection with the market conditions. **This provision violates Article 49.1 (Transfer of licenses) and Article 50.1 (Transfer of specific parts of the licensed area) of the Minerals Law.**

1.2 The Investment Agreement

This "Investment Agreement" (hereinafter "Agreement") is intended to be concluded by and among (1) the Government of Mongolia, (2) "Erdenes Tavan Tolgoi" (hereinafter "ETT"), a Mongolian state owned joint-stock company, (3) "Energy Resource Corporation", a 100 percent subsidiary of "Mongolian Coal Corporation", a Luxembourg corporation, (4) "Energy Resource" LLC (hereinafter "ER"), a 100 percent subsidiary of "Energy Resource Corporation", and (5) "China Shenhua Energy company limited" (hereinafter "Shenhua"), a Chinese state owned entity.

As stated in Articles 2.1 (c) and (d) of the Investment Agreement, ER has the full authority to determine the detailed mining work plan, operational expenses for construction and mining, investment conditions and scope of mining operations, to prepare calculations (budget) for mine development and exploration plans, to independently prepare plans, to make decisions related to all other activities of the project and take all necessary actions.

Moreover, ER has the right, on its own or independently, **to develop a feasibility study for the Mining Operation and to make changes and amendments to the feasibility study**, to determine the detailed mining plan, mine development programs, costs of mining operations and construction, terms and conditions of the investment, to export, sell, transport and market the Products produced and coals mined or extracted,. (Article 5.1 (b) of the Investment Agreement and Article 5.1 (d), (n) of the Cooperation Agreement)

[2] Translation note: competitive bidding – tendering process

In addition, ER has the right to **independently work on and determine decisions related to sales of products such as the volume and quantity of Products to be mined and processed** from Tsankhi Mine area **in any given year**, choosing the markets for the product sale, coal processing costs and rates, volume and price of Products to be sold, frequency of shipments and terms and conditions of transportation agreements and other commercial terms. (Articles 2.4 (b) and 2.5 (b) of the Investment Agreement)

The abovementioned provisions violate Article 48.6 of the Minerals Law under which the right to prepare a feasibility study and mining work plan as well as undertake mining exploration to upgrade the reserve during mining is kept with the license holder or ETT.

Based on these provisions [of the Investment Agreement], ER has the right to independently make decisions on increasing the project cost, and increasing or decreasing its investment by making amendments to the feasibility study. In particular, it allows ER to keep the project under its control for a longer term by inflating its exploration cost and claiming that it is not able to recover its investment. Furthermore, it appears from the provisions of the Investment Agreement that it is not possible for the Government and ETT to monitor and control such actions of ER.

1.2.2 Under Article 2.6 of the Investment Agreement which is titled “Railway base structure development”, ER will, alone, hold the special right to build, own, operate, and transfer the railway base structure and to undertake the railway transportation in the route of Ukhaa Khudag – Gashuun Sukhait for 30 years .

The Investment Agreement provides that ER may transfer 51 percent ownership of the Railway base structure to the State for free or without any consideration and sell the remaining 49 percent to the State. This does not comply with Article 6.2 of the Law of Mongolia on Railway Transportation.

Article 6.2 of the Law of Mongolia on Railway Transportation stipulates as follows: “Railway base structure that has special importance to the society and economy of the country shall be in the ownership of a State owned or predominantly State owned company or may be newly established subject to a condition for transfer to the ownership thereof after specific period of operation; and the direction of such base structure and railway line shall be determined by the Government”.

Under this provision, a newly built railway base structure must be transferred to the State after certain period of time and it implies “complete transfer” (not partial transfer). Therefore, ER must transfer the entire railway base structure in the direction of Ukhaa Khudag – Gashuun Sukhait to the State. In other words, “Energy Resources Rail” LLC (“ERR”) which is granted the concession right does not have the right to keep 49 percent of the railway and then sell it to the State.

The reason is that the railway base construction in the direction of Ukhaa Khudag – Gashuun Sukhait was determined as the base structure of special importance to the State by Article 1 of the Government Resolution number 121 dated 3 November 2012.

Therefore, Article 2.6 of the Investment Agreement titled "Railway base structure development" breaches Article 2.2 of the State Railway Policy, approved by the Parliament Decree #32 dated 24 June 2010, which provides that "new railway base structures that have special importance to the society and economy must be in the State ownership as provided in Article 6.2 of the Railway transportation law".

1.2.3 Article 2.7 (a) and (b) of the Investment Agreement provides that ER will build, own and operate power generation and transmission as well as water supply infrastructures and facilities required for the project.

Under these provisions, ER obtains a concession, but this issue cannot be resolved by this agreement, as the Government must decide concession according to the Law on Concession.

The granting of a concession right under this investment agreement breaches Article 6.1.2 of the Law on Concession and impinges on the authorities of the Government.

1.2.4 Under Article 5.3 (b) of Investment Agreement and Article 8.2 (c) of the Cooperation Agreement, ER has the right of first offer in the **event** ETT decides to **transfer** to any third party **and dispose of** the Tsankhi Mining Licenses in any manner.

Those provisions breach Articles 49.1 and 49.3 of the Minerals Law under which the license holder may transfer its license to (i) a newly established entity which succeeds its rights and obligations as a result of a merger and acquisition; or (ii) its parent company, or (iii) an entity which purchased its mine.

Furthermore, this provision conflicts with Article 1.a of the Government Resolution number 268 of 2014 with respect to "Some measures to take concerning the Tavantolgoi Deposit" which states that "[Tavantolgoi deposit] shall be used under "Investment and Cooperation Agreement" without transferring the mining license for Tavantolgoi deposit held by Erdenes-Tavantolgoi, a State owned entity".

The non-transferability of the mining license is the main condition for the cooperation with investors. Therefore, this provision should not be included in the Investment Agreement and the main requirement of the tender will be violated if the mining license is transferred to ER in any manner.

Moreover, under Article 8.2 (c) of the Cooperation Agreement, Parties must negotiate the purchase price [of the license] and if the Parties fail to agree on purchase price, the value of the Tsankhi Mining Licenses will be determined by an internationally recognized professional valuation firm. Then ER will be entitled to purchase at such price determined by the international firm. Although it is appropriate to have an international professional firm to valuate, it implies that ETT must sell the license only to ER at the determined value. This can be clearly seen from Articles 8.2 (b) and 8.2 (c) of the Cooperation Agreement which state that "it is prohibited to assign, novate or otherwise dispose the Tsankhi Mining Licenses to any third party without providing the right of first offer to ET".

Nonetheless, sections (i) and (ii) of Article 8.2 (d) of the Cooperation Agreement restricts ETT from selling or transferring the mining license to any third party. For instance, aforementioned provisions state that **ETT shall provide ER with a copy of the written agreement executed by ETT and the transferee**; and the transferee **and ER** will execute acknowledgement and accession deed, the **substance and form of which must be as reasonably requested by ER**, according to which the transferee must agree to be bound by the Cooperation Agreement and the Investment Agreement. In the event ER intentionally proposes a deed with the terms and conditions that are unable to accept for the transferee, any transaction for license transfer between ETT and a transferee will fail.

1.2.5 Under Article 10.1 (b) of the Investment Agreement and 5.1 (e) and 6.1 (i) of the Cooperation Agreement, ER has the right to own the coal mined from Tsankhi mine area.

Article 6.2 of the Constitution of Mongolia states that “the subsoil and its wealth shall be the property of the State” and Article 5.1 of Minerals Law further clarifies this provision by stating that “Mineral resources naturally occurring on the land surface and in the subsoil of Mongolia are the property of the State”.

Moreover, Article 5.2 of the Minerals Law states that “the State, as the owner, has the exclusive authority to grant the right for search, exploration and **use (i.e., mining) of** minerals according to the terms and conditions set forth in this law”. Accordingly, ETT, a State owned entity, has the right to use (i.e., mine) Tsankhi mine area of Tavantolgoi as the holder of the mining license. Based on the provisions of the Minerals Law, the State does not have the right to transfer the minerals ownership rights but it can only grant the right to use or mine minerals through licensing.

Therefore, ER does not have the right to own coal mined from Tsankhi mine area. Also Article 29.4 of Investment Agreement provides that “ER shall be an independent contractor ... under this Agreement”.

1.3 The Concession Agreement for “build-own-operate-transfer” of railway base structure

The “Concession Agreement for build-own-operate-transfer of railway base structure” (hereinafter the “Concession Agreement”) is proposed to be concluded by and among 4 parties which are (1) **the Government of Mongolia;** (2) **“Energy Resource Corporation”** (hereinafter “ERC”), 100 percent subsidiary of “Mongolian Coal Corporation” which is a Luxembrough corporation; (3) **“Energy Resource Rail” LLC** (hereinafter “ERR”), a subsidiary of “Energy Resource” LLC, which is in turn a 100 percent subsidiary of “Energy Resource Corporation”; and (4) **“China Shenhua Energy company limited”** (hereinafter “Shenhua”), a Chinese state owned company.

Under Article 10.4 of the Investment Agreement, Concessionaire (which is ERR) will retain the ownership right of the railway base structure in the direction of Ukhaa Khudag – Gashuun Sukhait. Appendix 4 of the Investment Agreement regulates right related to land. **As stated in this Appendix, the land for this railway concession is granted for 60 years subject to further extension.**

However, “MTZ” JSC, a State owned entity holds the license and concession right for building railway base structure for the same route.

Article 6.2 of the Law on Railway Transportation stipulates as follows: “Railway base structure that has special importance to the society and economy of the country shall be in the ownership of a State owned or predominantly State owned company or may be newly established subject to a condition for transfer to the ownership thereof after specific period of operation; and the direction of such base structure and railway line shall be determined by the Government”.

Article 2.2 of the State Railway Policy, approved by the Parliament Decree #32 dated 24 June 2010, provides that “new railway base structures that have special importance to the society and economy must be in the State ownership as provided in Article 6.2 of the Railway transportation law”.

According to the aforesaid provisions of the Railway transportation law and the State Railway Policy, there are 2 options: Railway base structure that has special importance to the society and economy of the country must be in the ownership of a State owned or predominantly State owned company, or a private party builds such railway structure and operate it with the condition to transfer it to the State after certain period of time.

The National Security Council of Mongolia issued Recommendation with number 35/32 in 2011 and Recommendation with number 07/04 in 2012 (*Copies of such recommendations are attached*), both of which comply with the aforesaid provision of the Railway transportation law.

Article 1 of the Recommendation with number 35/32 of 2011 provides that “the concession for new railway base structure that is stated in the “State Railway Policy” to be approved by the State Great Hural Resolution number 32 of 2010, will be granted to the State owned or predominantly State owned company pursuant to procedures described in Article 17.1.1 of the Concession Law”[3].

The Government of Mongolia determined that the railway base structure to be built in stages 1 and 2 /including the railway in the direction of Ukhaa Khudag - Gashuun Sukhait/ as the base structure of special importance to the economy and society of the country and granted the license for building base structure to the 100 percent state owned “MTZ” JSC by issuing a Government Resolution with number 121 dated 3 November 2012 in accordance with Article 6.2 of the Law on Railway Transportation and the Recommendation of National Security Council of Mongolia. (*The Government Resolution number 121 in 2012 is attached*)

Furthermore, under the Government Resolution number 28 dated 26 January 2013, the concession of build-operate-transfer of railway base structures (including the

[3] Concession Law

17.1. A concession can be granted by concluding a direct agreement under the following circumstances:

17.1.1. when it is deemed that conducting a tender would jeopardize national security.

direction of Ukhaa Khudag – Gashuun Sukhait) to be built under the 1st and 2nd stages of the State Policy on Railway Transportation was granted to "Mongolian railway" JSC.

In other words, the National Security Council of Mongolia issued a recommendation on the basis of the consideration that granting the license and the concession for building base construction of new railway in Mongolia under tender would contradict with the national security and the Government of Mongolia granted the license for building new railway. Accordingly, the concession of railway base construction to the state owned "MTZ" JSC based on such recommendation.

The Recommendations of the National Security Council with numbers 35/32 of 2011 and 07/04 of 2012 that were unanimously approved by Ts.Elbegdorj, the President of Mongolia, D.Demberel, the Speaker of the Parliament and S.Batbold, the Prime Minister, are still valid. Furthermore, the Government Resolutions with numbers 121 of 2012 and 28 of 2013 under which the license and concession for building railway base structure in such direction were granted to "MTZ" JSC are also valid as of today.

Moreover, the meeting of National Security Council was held on 16 February 2015 with respect to Tavan Tolgoi and it directed to conclude Tavan Tolgoi Agreement in compliance with the Investment Law and relevant laws of Mongolia and to enhance the correlation among resolutions and decisions previously issued by the Parliament and the Government in relation to utilization of Tavantolgoi deposit.

The Government has an obligation to implement decisions of National Security Council pursuant to Article 27.1 of the Law on Government which states that "The Government shall take measures to implement a decision of National Security Council … and report such measures to the President".

Therefore, there is no legal ground for the Government to make a decision to take back from the state owned "MTZ" JSC and transfer to the other legal entity the right and concession of building the railway base structure in the direction of Ukhaa Khudag-Gashuun Sukhait.

D.Ganbat, the Executive Director of "MTZ" JSC, has notified M.Enkhsaikhan, the Minister of Mongolia and relevant officials of the Parliament and Government of this matter by its official letter with number 01/281 dated 3 April 2015 (Official letter with number 01/281 of 2015 of the Executive Director of "MTZ" JSC is attached).

The transfer of railway base structure in the direction of Ukhaa Khudag – Gashuun Sukhait to the private company with foreign investment as part of the tender violates the National Security Council's Recommendations with numbers 35/32 of 2011, 04/03 of 2015, Clause 2.2 of the Parliament resolution #32 dated 24 June 2010 under which the State Railway Policy was approved, Government resolutions with numbers 121 dated 3 November 2012 and 28 dated 26 January 2013

Two. Whether the Agreement is in compliance with the valid resolutions issued by the Parliament and relevant Standing Committees on the subject matter,

2.1 The Project Company that is intended to be established by “Energy Resources LLC” (ER), “Energy Resources Corporation” (ERC), and “China Shenhua Energy Company Limited” (Xinxua) jointly is actually “Energy Resources” LLC that is operating in the Ukhaa Khudag Deposit at the moment. In other words, ERC is converting its own subsidiary company Energy Resources into the Project Company.

“Energy Resources Corporation” (ERC) will hold 51% and “China Shenhua Overseas Development & Investment Company Limited” (Shenhua) will hold 49% of “Energy Resources”, a company which is converted into the Project Company. (Article (H) of the General conditions of the Investment Agreement)

ER is a legal entity with foreign investment in accordance with Article 3.1.5 of the Investment Law which states that “a business entity with foreign investment” means a legal entity incorporated under the laws of Mongolia, and 25 percent or more of total issued shares of the legal entity is held by a foreign investor and the amount of investment made by each investor is US$100,000 or more (or equivalent in Mongolian togrogs) because “Energy Resources Corporation”, a parent company of ER, is 100% owned by investor of Luxembourg.

“Energy Resources Corporation” is 100 percent owned by foreign investor and “Shenhua” is a foreign legal entity, thus a joint venture company ER which is called the Project Company to operate Tavantolgoi deposit, directly and indirectly, lies under the control of foreign legal entities.

It violates Clause 2.1 of “General principle and guideline for concluding the investment agreement to jointly operate the Tavantolgoi coal deposit” approved by Annex 1 of the Parliament Resolution # 40 dated 04 December 2008 which states that “to consider the possibility of owning not less than 51 percent of the joint stock company to be established in relation to the deposit by the Mongolian side”

Furthermore, it directly violates Article 1.1 of the Parliament Resolution # 39 dated 7 July 2010 which states that “State owned company shall carry out mining operation on the Tavantolgoi coal deposit, …”.

“General principle and guideline for concluding the investment agreement to jointly operate the Tavantolgoi coal deposit” approved by Annex 1 of the Parliament Resolution # 40 dated 04 December 2008 and their implementation can be seen from a table below:

GENERAL PRINCIPLE AND GUIDELINE FOR

CONCLUDING THE INVESMENT AGREEMENT TO JOINTLY OPERATE

THE TAVANTOLGOI COAL DEPOSIT

AND ITS IMPLEMENTATION

No	Articles of the General principle and guideline for concluding of	Draft Investment Agreement to be concluded with the Consortium which

	investment agreement to jointly operate the Tavantolgoi coal deposit	**obtained the tender offered under the Government Resolution #268**
1	To conclude the Agreement in compliance with the effective laws and legislations	Violated effective laws and legislations of Mongolia.
2	To consider the following alternatives when concluding the Agreement: 1/ Mongolian side owns not less than 51% of the joint stock company to be established in relation to the Tavantolgoi coal deposit; 2/ based on product sharing principle.	It does not satisfy the requirement that Mongolian side's participation to be not less than 51% since "Energy Resources Corporation" with 100% investment by Luxembourg holds 51% of the Project Company which will operate Tavantolgoi deposit. No Product sharing principle is negotiated.
3	To agree in the Agreement that definite parts of the royalty for mining and tax to be paid in advance.	Agreed to receive an advance payment of USD200 million with the interest of 4.5% per year. This payment will be withheld from the cooperation payment and taxes to be paid in the future.
4	To agree that the investment by Mongolia can be in a form of royalty for mining, tax, fee, dividend, and loan etc.,	Agreed that Mongolia will not make any investment because 51% of the Project Company which operates the Tavantolgoi deposit is held by 100% foreign invested company "Energy Resources Corporation LLC" and 49% is held by the state owned "Shenhua" company of PRC.
5	To include in the Agreement solution for new infrastructure buildings such as power plant, road, railway, water supply building and town or village, social and cultural issues in relation to the use of the deposit.	Article 2.6 of the Investment Agreement provides the matter about building-owning-operating-transferring of railway and Article 2.7 provides the matter about building-owning-operating of power generation and water supply infrastructure. Further, Article 16.2 states that a Cooperation Agreement on Regional Development will be concluded with the Local administration organization. No specific provision in relation to the town or village and social, cultural issues.
6	To adhere a principle of producing final product and agree on stages and types of productions to be produced.	No negotiation was made in relation to the final production.
7	To agree on program and plan for preparing national human resources to work in the industry.	Article 5.9 of the Investment Agreement states that "……shall be entitled to engage its own employees freely at its own discretion and employ them under an employment contract", " … shall hire citizens of Mongolia who meet the relevant requirements for work place…", "…shall consider about hiring citizens of gobi region, especially citizens of Umnugobi aimag will be in a high priority".
8	To include in the Agreement about use	Article 16.3 of the Investment Agreement

	of latest top techniques and technologies without damage to the environment, human and animals; and performing the environmental rehabilitation operation in every stage of the exploration and mining of the deposit.	provides that the obligations in relation to the environment, health, safety procedure and social relations will be fulfilled. There is no provision about using latest top techniques and technologies without damage to the environment, human and animals.
9	To take into the account the experience in mining sector, financial capacities of the foreign and national reliable companies and offers made by them when concluding the Agreement.	Shenhua of PRC, Peabody of the USA, Itochu, Marubeni, and Sojitzu of Japan, the investors expressed its interest in tender, have the experience in mining sector and have financial capacities. However, the shares of "Energy Resources Corporation" which owns 51% of the Project Company, is pledged in favor of its parent company and Cayman company MMC for loan. It violates the guidance approved by the Parliament because the company which is financially incapable owns 51% of the Project Company that might operate the Tavantolgoi.
10	To get an assistance from an internationally recognized advisory entity for drafting the Agreement.	The Government did not receive an assistance from an internationally recognized advisory entity when preparing the draft Agreement. The Minister M.Enkhsaikhan responded to the particular parliament members who sought clarification on this that "The investors are receiving legal services from "Devis Polk" and "King & Woods Mallesons", and financial services from "Deloitte" and "KPMG". **For the Mongolian side**, the working group considers that the capacity of the governmental organizations is sufficient thus **will not hire foreign companies or counsels**".

2.2 Under Article 2.1 (b) of the Cooperation Agreement, ER's purpose is not only to carry out mining but also conduct development, construction, ownership, operation and maintenance of a coal handling and processing plant, power generation and transmission infrastructure and facilities, water supply infrastructure, facilities, and services for railway base structure and railway transport operation, power and water supply, transportation, all sales operations and other operations in relation to the mining operations.

Moreover, under Articles 2.1 (b) and 2.2 (a, c) of the Investment Agreement, ER will carry out coal mining, coal processing, disposing, transporting, exporting, selling, trading and marketing, and collecting using and spending of coal sales revenue, planning the mine and reporting to the

authority, raising fund, investing, creating security interest, constructing the railway, handling railway transportation operation and management, constructing coal processing plant, water and power supply facilities, using and mining the reserves found during additional exploration, and constructing ancillary infrastructure at Tavantolgoi Deposit.

These provisions contradict with the statement regarding the **mining** operation for the purpose of operating the Tavantolgoi Deposit stated in the Action Plan of the Government of Mongolia for 2012-2016 approved by the Parliament Resolution # 37 dated 18 September 2012.

Mining operation is an activity of a contractor that extracts underground coal to the ground surface but not such wide range operation as written above.

Accordingly, Article 1/1 of the Resolution #39 dated 7 July 2010 states that "A stated owned company to conduct mining operation at Tavantolgoi coal deposit, to establish "Erdenes Tavantolgoi" joint stock company in accordance with the relevant laws and legislations, and transfer mining license for operating the deposit to it without separation, to enter into an investment agreement with it, and to have an operator entity for carrying out mining operation for certain period".

2.3 The Government did not implement Article 1.2 of the Resolution # 05 of the Petition Standing Committee of the Parliament dated 18 February 2015 which states that "To include a specific chapter in the agreement to be concluded with the investors of Tavantolgoi Deposit and ensure inclusion of necessary regulations on protecting the interests of the citizens who hold 1072 shares of the Tavan Tolgoi JSC and maximizing their benefit from such shares".

2.4 Article 6.2 of the Law on Railway Transportation provides that: "Railway base structure that has special importance to the society and economy of the country will be in the ownership of a State owned or predominantly State owned company or can be newly established subject to a condition that such railway base structure will be transferred to its ownership after specific period of operation; and the direction of such base structure and railway line will be determined by the Government".

The railway base structure in the direction of Ukhaa Khudag – Gashuun Sukhait was determined as the base structure of special importance to the State by Article 1 of the Government Resolution with number 121 dated 3 November 2012.

Granting of the concession right to build-own-operate-transfer for the railway base structure in the direction of Ukhaa Khudag – Gashuun Sukhait to the private company "Energy Resources Rail" LLC, a subsidiary of the foreign invested company, for a term of 30 years breaches Article 2.2 of the Parliament Resolution #32 of 2010 under which State Railway Policy was approved /"a railway base structure to be built newly that has special importance to the society and economy must be in the ownership of the State as provided in Article 6.2 of the Law on Railway Transportation". (*Detailed explanation is provided in part 1.3 titled "Concession Agreement for "building- -operating- owning- transferring" of railway base structure"*)

Three. Whether the Agreement complies with the National Security Concept, Recommendations by the National Security Council, relevant Government decisions and other decisions of the governmental authorities,

3.1 Article 3.2.2.2 of the National Security Concept approved by the Parliament Decree #48 of 2010 states that "Design a strategy whereby the investment of any foreign country does not exceed one third of overall foreign investment in Mongolia. Undertake a policy to restrict investments by foreign state-owned companies and balance the volume of investments by neighboring and highly developed countries within strategically important sectors".

The total investment in the Project is approximately USD4 billion as stated in Article 2.8 (a) of the Investment Agreement for operating Tavantolgoi coal deposit.

The Gross Domestic Production of Mongolia is approximately USD11 billion and the investment almost equal to 40% of GDP to be made by one joint venture company in which the state owned company of PRC is participated. This will trigger a non-compliance with Article 3.2.2.2 of the "National Security Concept" under which a policy to balance the amount of investments by neighboring and highly developed countries must be adhered.

3.2 In our view, the matter related to the concession for building- operating-owning= transferring of railway base structure in the direction of Tavan Tolgoi – Gashuun Sukhait is an integral part of the national security and national interests.

The following provisions in the National Security Concept approved by the Parliament Resolution #48 of 2010 should be adhered for developing cross-border infrastructure and minerals sector.

Article 3.1.2.5 of the "National Security Concept" states that "Border area regional economies shall be developed in accordance with unified national interests, Mongolia's sovereignty, inviolability of borders and territorial integrity"; Article 3.1.2.7 states that "Border area development strategy and its foreign connections shall be defined and regulated by unified state policy"; Article 3.2.1.4 states that "Infrastructure industry development shall be linked to national security requirements while economic efficiency shall be a criterion for making investments. Primacy of Mongolia's national interests shall be the guiding principle when developing the nation's railway network"; Article 3.2.4.1 states that "While developing the mineral resource sector give importance to ensuring national security so as to avoid becoming merely a commodity supplier or an arena of confrontation of conflicting interests among national and foreign political interests or businesses, as well as giving importance to preventing environmental degradation. Improve mining sector transparency and responsibility as well as overseeing mining industry incomes"

The above Articles of the National Security Concept and State Policy on Railway Transportation indicates the significance of railway base structure with social and economic importance to the national interest of the country.

Granting the railway base structure in the direction of Ukhaa Khudag – Gashuun Sukhait to the private company "Energy Resource Rail" LLC, a subsidiary of the foreign invested company, for 30 years under the condition of building-owning-

operating-transferring and concluding agreement for building-owning-operating-transferring breaches Article 2.2 of the Parliament Resolution #32 dated 24 June 2010, Articles 3.1.2.5, 3.1.2.7, 3.2.1.4 and 3.2.4.1 of the National Security Concept approved by the Parliament Resolution #48 of 2010, The National Security Council's Recommendation #35/32 of 2011, Government Resolution #121 dated 3 November 2012, Government Resolution #28 dated 26 January 2013 respectively. (*Detailed explanation is provided inpart 1.3 titled "Concession Agreement for "building-operating- owning-transferring" of railway base structure"*)

On 16 February 2015, the meeting of National Security Council was held with respect to Tavan Tolgoi and it directed the Government to conclude Tavan Tolgoi Agreement in compliance with the Investment Law and other relevant laws of Mongolia so as to enhance the correlation among resolutions and decisions previously issued by the Parliament and the Government in relation to utilization of Tavantolgoi deposit take measures with the aim of providing the citizens of Mongolia who hold the share of "Erdenes Tavan Tolgoi" JSC with the possibility of obtaining dividend by way of circulating it into economic. However, the Government failed to implement this recommendation.

The Government is obligated to implement the decisions of National Security Council under Article 27.1 of the Law on Government which states that "The Government shall take measures to implement the decision of National Security Council … and report such measures to the President". (*The Recommendation #04/03 of the National Security Council of 2015 is attached*)

3.3 The Minister M.Enkhsaikhan did not take advisory service which leads to violation of Article 10 of the "General principle and guideline for concluding the investment agreement to jointly operate the Tavan Tolgoi Coal Deposit" approved by the Parliament Resolution # 40 dated 04 December 2008 which requires "to take an advice from internationally recognized advisory services organization in preparing the draft agreement".

Consequently, Article 10 of the Parliament Resolution # 40 of 2008 has not been implemented. (*The Parliament Resolution # 40 of 2008 is attached*)

The Minister M.Enkhsaikhan responded to the particular parliament members who sought clarification on this. He said that "The investors are receiving legal services from "Devis Polk" and "King & Woods Mallesons", and financial services from "Deloitte" and "KPMG". For the Mongolian side, the working group considered that the capacity of the governmental organizations was sufficient thus [they] would not hire foreign companies or counsels".

The Government of Mongolia lost its opportunity to be legally protected in the agreement within the frame of the laws as it did not hire the professional legal and financial counsels.

3.4 The Minister M.Enkhsaikhan, leads the negotiation however it violates Article 4 of the minutes of the National Security Council's meeting dated 18 May 2010which states "to adhere a principle that … to keep the negotiation within proper professional level and to prohibit any political official to take part in any of the

negotiating parties". (*Minutes of the National Security Council's meeting dated 18 May 2010 is attached.)*

3.5 Article 27 of the Investment Agreement states that "This Agreement shall be executed in both English and Mongolian languages and in case of any discrepancies, the English language version shall prevail". The Mongolian version of the Agreement is a translation of its English version. It appears that the Agreement is originally drafted in English and it is being translated into Mongolian.

A dispute in relation to the Agreement will be resolved by an arbitration in London in English language. But it is not in compliant with the guidance stated in the minutes of the meeting #24/11 of the National Security Council dated 10 May 2010 which provides that "The tender documents for choosing strategic investors of Tavan Tolgoi, draft agreement and other related documents should be drafted in both Mongolian and English languages without mistake".(*Minutes of the National Security Council's meeting is attached.*)

Four. Whether the Agreement is in compliance with third neighbor policy of Mongolia,

4.1 Under Articles 12.3 (a), (b), 12.4 (a), ER will establish a trading joint venture and 75% of the products will be traded to PRC and 25% will be traded to the third market through the Trading company. 30% of the shares in such trading company will be held by Japanese partner, the member of the Consortium.

As per this article, "Sumitomo" corporation of Japan is neither an investor of the Project Company ER operating the Tavan Tolgoi Coal Deposit or the owner of the railway base structure ERR, , but it is only a partner of the Trading company.

The Ministry of Foreign Affairs developed a memorandum of understanding on "Third neighbor" policy. The Government discussed it and approved it upon reflecting the recommendation of National Security Council. Then the Ministry of Foreign Affairs delivered it to Ts.Enkhtuvshin, the secretary of the National Security Council by its official letter number N/89 dated 25 April 2014.

"Sumitomo" corporation of Japan has no participation in either Project Company operating the Tavantolgoi deposit or the company owning the railway base structure. It is not in compliance with Articles 2.1, 4.6, 4.10 and 4.11 of this Memorandum of Understanding.

4.2 Article 12 of the Cooperation Agreement titled "Confidentiality" and Article 29.3 of the Investment Agreement titled "Confidentiality" refer to Stock Exchanges in Hong Kong and Shanghai, only.

We think that these Agreements intentionally exclude the involvement of internationally recognized Stock Exchanges of our third neighbor countries such as Stock Exchanges of London, New York, Tokyo and Toronto for the operation of Tavan Tolgoi and issuance of the securities during the term of the Agreement.

4.3 As “Sumitomo” of Japan is not directly participating in the project for operating the Tavan Tolgoi Coal Deposit, it does not satisfy Article 3.1.1.5 of the National Security Concept which provides that “to develop bilateral and multilateral cooperation with high developed, democratic countries in the fields of politics, economy, culture, and humanity within the third neighbor policy”.

The Cooperation Agreement, Investment Agreement and Railway Concession Agreement for operating the Tavantolgoi deposit do not satisfy the real participation and investment by the Third neighbor and do not comply with the Third neighbor policy which is a part of the foreign policy of Mongolia.

Five. Whether it correlates with the business interests of “Erdenes Tavan Tolgoi” state owned JSC,

5.1 About the influence on Erdenes Tavan Tolgoi JSC’s business operation,

5.1.1 Under Part D of the Recitals and Articles 1.1 (a), 1.1 (b), 1.2 (a), and 6.1 (d) of the Cooperation Agreement, ETT transfers **all of its rights** and some certain obligations **related to the mining operation** under its **mining license** for Tsankhi and **all its rights related exploration and complete mining operation** as well as its **land possession right** to ER for the total Term of this Agreement (main Term of the agreement is 30 years subject to extension of another 30 years).

Under abovementioned provisions, ER will indirectly have the real and complete controlling right over Tavantolgoi deposit for 60 years upon transfer of all rights in relation to the mining license, land possession right, all rights regarding the mining operation by ETT to ER.

5.1.2 Under Part E of the Recitals and Article 5.1 (q) of the Cooperation Agreement, ETT transfers certain of its obligations and **assets** including current **employees** working in Tsankhi mine area, contract for sale of coal from Tsankhi mine area and contract for mining services, and other contracts to ER and agreed to conclude an “Assignment Agreement” separately.

The matter in relation to the transfer/assignment of assets, certain obligations, and employees of ETT to another company must be resolved under Article 87 (Major Transactions) of the Company Law. However, ETT has not made its decision in accordance with Article 87 (Major Transactions) of the Company Law. Concluding the “Assignment Agreement” prior to such decision will breach Article 87 of the Company Law in its entirety.

5.1.3 Articles 1.1 (a) and 2.3 (c) of the Investment Agreement provides that “**Tsankhi Mine area will be developed by corresponding coal of Tavan Talgoi Deposit with Ukhaa Khudag deposit,** and to combine coals extracted from mines at Tsankhi Mine area with other coals mined from different mines at Tavan Tolgoi area; and both ETT and ER hold the mining license for Tsankhi Mine area and Ukhaa Khudag Deposit for initial 30 years subject to 20 years of extension two times which means the mining licenses have to be effective for a total of 70 years in accordance with Article 5.2 (a) of this Agreement.

Furthermore, the terms of the Investment Agreement will also apply to the operations in relation to the Ukhaa Khudag Deposit during the terms of the Investment Agreement as stated in Article 5.2 (e) of the Investment Agreement.

The operation of Ukhaa Khudag deposit which is owned by the private company should not be covered under Investment Agreement or other ancillary agreements for operating Tavantolgoi deposit and the Government should not bear the obligation in relation to Ukhaa Khudag Deposit. Since the Ukhaa Khudag Deposit is not an item of the Investment Agreement, the provisions related to Ukhaa Khudag Deposit need to be removed from the Investment Agreement.

ETT owns assets with approximate value of USD10 billion and has 592 employees.[4]

ETT is carrying out normal operation by mining 5.3 million tons of coal in 2013 and 4.5 million tons in 2014. ETT is a huge competitor of ER because they operate at the same market by producing same type of product. Tavan Togloi Deposit, possessed by ETT, has 7.4 billion tons[5] of reserves while ER's "Ukhaa Khudag Deposit", has approximately 400 million tons of reserves.

ETT is the state owned company that operates on the Tsankhi Mine area of Tavan Tolgoi and it will be not possible to earn a profit by transferring all its operating right to ER. ETT will not be possible to earn profit as it transfers its core mines of east and west Tsankhi, together with whole mining operations to ER.

Therefore, ER creates to itself favorable business condition by way of disabling its competitor who owns a bigger deposit.

5.2 About debts owed to "Chalco", a company of PRC

5.2.1 The general regulation about the settlement of Chalco debt is stated in Article 8.3 of the Cooperation Agreement. Under Article 3.4 (a) of the Investment Agreement, it is clearly stated that **ER shall independently decide whether to pay** the Chalco debt of USD142 million within 12 months **either by way of supplying products or in cash**.

If ER pays the Chalco debt by supplying coal, basically there is no difference because ETT is still paying its debt to Chalco by supplying coal and the debt can be fully paid in such way. When the working committee visited and worked at the Erdenes Tavan Togloi JSC's mine site on 15 June 2015, there was 2.3 million tons of coal prepared for export and 2 million tons of coal uncovered and ready for extraction.

It shows that ETT has full capacity to pay the Chalco debt by working its normal performance since there is total of 4.3 million tons of coal and its current value is USD150 million if consider that the price for one ton is USD35.

[4] 199 employees are working at the office, and 473 employees of 5 departments are working at the mine of "Erdenes Tavan Tolgoi" JSC.

[5] The geological reserves of coal of Tavantolgoi deposit is total of 7,4 billion tons carbonized and energy coal in accordance with reserve estimation transferred to international Jork classification made by "Norvest" company.

5.2.2 **Article 3.4 (b)** of the Investment **agreement** states that "ETT shall solely be liable for any debts other than those specified in Article 3.4. (a) (this clause states only about Chalco debt) of this Agreement".

Furthermore, under Article 3.8 of the Investment Agreement and Article 4 of its Appendix 3 thereof, either Government or ETT shall not be entitled to demand ER to pay any other payments. Moreover, as stated in Article 3.3 of the Cooperation Agreement titled "No further obligations", ER shall not be responsible for any other debt, payment, taxes, fees or salary payable by ETT **other than the Chalco debt**.

The Consortium's approach is not fair, because it illustrates that it will only pay liabilities the Chalco debt without any other payments and debts. ETT owes USD250 22million to the Development Bank of Mongolia, approximately USD30 million to the domestic banks, and MNT30-50 billion to others.

It is not clear how ETT will pay its debts because under the Investment Agreement and other related agreements, ETT is about to transfer all of its rights to "investors" and is becoming unable to operate its main deposits that are being operated normally.

Therefore, the issue related to the debts payable by ETT to others should be settled together. For instance, there is an outstanding debt to "TTJVCo", a company that is a subsidiary of Australian "Macmahon" company, which operates mining activity at the east Tsankhi Mining. If such debt and payment issues are not settled, this company may submit a complaint to the international arbitration and there is a high risk that the Government will probably be ruled to pay a million dollar in debt inclusive of interest and damage.

Moreover, "Mongol Uurkhachid Tunshlel"[6] and other 13 subcontractors operate at the west Tsanki Mining. They will claim a compensation if the contracts concluded with them are terminated.

Six. How the requirements for conditions of trading the company's shares on the international Stock Exchange are satisfied,

Under Article 1.2.в [c] of the Parliament Resolution # 39 dated 7 July 2010, the Government is obliged "To attract necessary investment by way of trading up to 20 percent of the shares "through domestic and international stock exchanges".

Moreover, Article 1 of the Minutes number 52 of the Government meeting organized on 9 November 2011 provides that "In view of the proposal of the working group on the restructuring and selection of stock exchange, the proposal for partial share issuance by ETT on each of Mongolian, London and Hong Kong Stock Exchanges have been supported".

Furthermore, the Parliament Resolution #37 titled "Approving the Action Plan of the Government of Mongolia for 2012-2016" dated 18 September 2012 states that "… further, to organize the trade of the shares on domestic and international stock

[6] "Mongol Uurkhachid Tunshlel" includes Mongolian national company "Khishig Arvin Industrial" LLC (with 450 employees), "MNO" LLC (with 70 employees), and "MERA" LLC (with 78 employees).

exchanges relying on the Tavantolgoi deposit in accordance with the Parliament decision".

However, the Government has failed to implement its obligation to attract necessary investment by trading up to 20 percent of the shares of "Erdenes Tavan Tolgoi" JSC on domestic and international stock exchanges.

There is no regulation is included in the draft of the Cooperation Agreement and Investment Agreement to be concluded with the Consortium, which passed the tender organized under the Government Resolution 268 of 2014in relation to trading of ETT Company's shares on stock exchanges.

If the Government could attract the necessary investment by trading up to 20 percent of ETT Company's shares on domestic and international stock exchanges, 3 billion (20 percent of the 15 billion shares is equal to 3 billion) shares could be offered and MNT3 trillion (USD1.5 million if 1USD is equal to MNT2000) could have possibly been raised if the market price per share was considered at MNT1000.

Example of the locally owned "Tavan Tolgoi" JSC's operation

The example of how the nominal value of shares of locally owned "Tavan Tolgoi" JSC (known as small Tavan Tolgoi) has been increased on the Mongolian Stock Exchange should be taken into account.

"Tavan Tolgoi" JSC is located in Tsogttsegtii soum of Umnugobi aimag in 100 kilometers of Dalanzadgad city and its main operation is mining and trade of coal and coke.

The company was incorporated as a local ownership predominated company by the Order number 42 of 1994 issued by the Government Privatization commission with 526,652 common shares issued with par value of MNT100 of which 49 percent was initially offered to public through "Mongolian Exchange" JSC starting from 03 April 1995. At that time, share values per share were MNT60, MNT40 and MNT16 at the initial market, respectively.

"Tavan Tolgoi" JSC peeled off 9.3 cubic meter overlay soil and extracted 3.1 million tons of coal in 2013 and this amount is greater by 823.0 thousand tons than extracted amount in the same period of 2012. In 2014, the company mined and traded 554.5 thousand tons of coal. Also it peeled off 4.6 million cube meters of overlay soil as shown in its shareholders meeting materials.

Depending on financial results of its operation, "Tavan Tolgoi" JSC distributed a total amount of dividend of MNT237.6 billion to its shareholders in 14 times during the period of 1996-2014.

Dividends distributed by the company shown below year by year (information was provided by Financial Regulatory Commission's official letter with number 2/3084 dated 16 June 2015):

No	Years of dividend	Amount of dividend per share /by togrog/

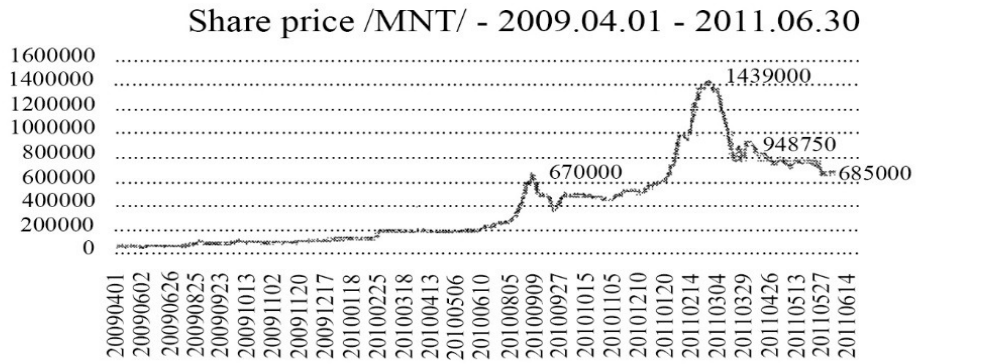
	distribution	
1	1996	0.18
2	1997	0.66
3	1998	8.06
4	2002	2.42
8	2004	949.39
6	2005	2,819.71
7	2006	6,467.37
8	2007	18,318
9	2008	18,381
10	2009	55,000
11	2010	130,000
12	2011	1,368
13	2013	766*
14	2014	59
15	**Total amount**	**234,139.79**
16	**Number of shares**	**52,665,200.00**
17	**Total amount**	**237,650,024,447.08 togrog**
		www.mse.mn

The Shareholders' Meeting of "Tavan Tolgoi" JSC made a decision to increase the amount of dividends of 2013.

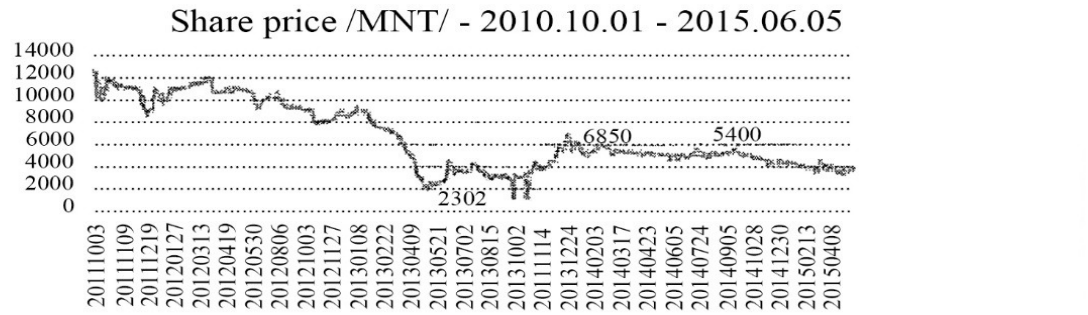
Locally owned "Tavan Tolgoi" JSC's market capitalization and share value.

As of 14 June 2015, market capitalization of "Tavan Tolgoi" JSC's is MNT226,776,351,200 on the Mongolian Stock Exchange. Information of the share price of the company is shown below in two parts as per the graphics from 01 April 2009 until and after the change in share structure.

Graphic No 1



Graphic No 2



The study of "Tavan Tolgoi" JSC's share value indicates that the peak of share price of the company occurred around March 2011 which was MNT1,439,000. Currently price per share is MNT4,306 and can be considered that price per share of the investment certificate is MNT430,600.

This history of "Tavan Togloi" JSC shows that there is a huge potential for ETT. Therefore, it can be estimated that profit from and market capitalization of the Tavan

Tolgoi will be very high since 7.4 billion tons of coking coal and coal for electricity generation can be mined from just 300 meters depth thereof.

Concluding the Investment Agreement and other ancillary agreements with Consortium in a form suggested by the Government which is not beneficial to ETT for the term of 30 years, and transferring all operational rights of "Erdenes Tavan Tolgoi" JSC to ER in a result of which it will be a "company on paper" decreases the value of the company and disables the opportunities to trade its shares on domestic and international stock exchanges.

Seven. Whether the interests of citizens and national business entities that hold 1072 shares of "Erdenes Tavan Tolgoi" JSC are secured,

Pursuant to Parliament Resolutions # 39 dated 7 July 2010, and #18 dated 16 February 2012, it was decided that up to 20 percent of the total issued shares of "Erdenes Tavan Tolgoi" JSC should be allocated to all the citizens of Mongolia in equal numbers for free of charge; and up to 10 percent of the total shares should be traded in equal numbers to the national entities by their nominal value.

"Erdenes Tavan Tolgoi" JSC issued 15 billion shares with nominal value of MNT933 per share. Total value of the company is MNT14 trillion.

Under Article 1 of the Government Resolution number 181 dated 30 May 2012, 1072 shares of the company was adjusted to MNT1 million and a nominal value per share was determined atMNT933.

According to the Financial Regulatory Commission's information, 12,433,326,819 shares representing 82.89% of the total ETT's shares are held by State of Mongolia while 2,558,175,510 shares representing 17,05% of the total ETT's shares are registered under the names of 2,475,201 citizens and 8,497,671 shares representing 0.06% of the total ETT's shares are registered under the names of 553 entities.

Under Article 4 of the National Security Council's Recommendation with number 04/03 dated 16 February 2015, the Government is obliged to "organize "Erdenes Tavan Tolgoi" JSC's shares to be traded in the market and take a measure to satisfy the condition to obtain dividend from these shares". However, such obligation was not fulfilled.

The Government failed to implement the Resolution # 05 of the Petition Standing Committee of the Parliament dated 18 February 2015 which requires "To include a specific chapter in the agreement to be concluded with the investors of Tavantolgoi deposit which must provide the regulations on protecting the interests of the citizens who hold 1072 shares of the Tavan Tolgoi JSC and satisfying the condition to get the economic benefit from such shares". (A *copy of the Resolution # 05 of 2015 issued by the Application Standing Committee of the Parliament is attached*)

Furthermore, Z.Narantuya, the Chairman of the Financial Regulatory Commission, delivered the Proposal and recommendation to the Government and Minister M.Enkhsaikhan with an official letter #1/1133 dated 16 February 2015 in relation to ensuring the rights of the citizens who hold 1072 shares of "Erdenes Tavan Tolgoi" JSC. (Chairman of the FRC *Z.Narantuya's official letter number 1/1133 dated 16 February 2015 is attached*)

However, the Government did not take any measures according to the recommendations of the National Security Council or the Financial Regulatory Commission, or the resolution of the Parliament's Petition Standing Committee.

Neither Cooperation Agreement nor Investment Agreement provide a regulation on trading of 1072 shares held by the citizens and shares held by the national business entities in "Erdenes Tavan Tolgoi" JSC or any regulation on ensuring their rights.

Therefore, the Working group is of the view that the Parliament Resolution to provide a provision to oblige the Government to include the trading of 1072 shares held by the citizens and shares held by the national business entities in "Erdenes Tavan Tolgoi" JSC and regulation ensuring their rights must be included in the Agreement for use of Tavantolgoi deposit.

Eight. Review of the legal grounds of the Government Resolution number 181 of 2012 that limits the voting rights of citizens who hold 1072 shares in "Erdenes Tavan Tolgoi" JSC

Under Article 3 of the Government Resolution with number 181 dated 30 May 2012, it was decided that 1072 shares held by the citizens and shares held by the national entities in "Erdenes Tavan Tolgoi" JSC shall not have any voting right.

This Government Resolution violates Article 5.2 of the Constitution of Mongolia which states "The State recognizes any form of public and private property and the rights of the owner shall be protected by law", and Article 5.3 thereof states "Owner's right may be limited exclusively on the grounds stated by law".

With his official letter with number 1/4087 dated 6 May 2015, Z.Enkhbold, the Speaker of the Parliament warned the Government that the Resolution with number 181 dated 30 May 2012 violated the Constitution. Similar warning was also served by Z.Narantuya, the Chairman of the Financial Regulatory Commission, under her official letter with number 1/2124 dated 21 April 2015. (Copies of the official letters are attached)

Therefore, the members of the working group are of the view that the relevant provision of the Government Resolution number 181 of 2012 should be invalidated and propose a draft Parliament Resolution for discussion.

Nine. Whether the Agreement satisfies the international cooperation principle of equality and mutually benefit

9.1 Under Articles 2.3 (a) and 3.1 (a) of the Cooperation Agreement, ER will pay ETT the certain percentage of the income from Mining Operation in accordance with agreed methodology (For instance: Cooperation payment equal to 2% when coal price is less than USD85) for granting the right to carry out the mining operation within the scope of mining license for Tsankhi. As stated in Article 3.2 (c) of such Agreement, ETT will be responsible for taxes and fees including mining license free, air pollution fee and royalty etc.

As stated in Article 3.1 (c), this methodology and percentage will not be changed and will be stable during the term of the agreement. In other words, it will be fixed for 30 years during the term of the agreement (subject to extension of 30 more years).

As stated in Article 2.5 (b) of the Investment Agreement, ER is defining the sales price, this Cooperation Payment cannot be estimated. Since there is no competitor that supplies at same market, there is no real possibility to keep the price high enough. We consider that ER owns the option to keep the coal price for less than USD 85.

9.2 As stated in Articles 5.1 (a) and 6.1 (g) of the Cooperation Agreement, ER has the right to have full access to and control over the Tsankhi mine area without any restriction. Contrary, ETT will have the right **to access the mine area upon prior consent of ER in order** to ensure whether ER is in compliance with the terms and conditions of the agreement.

As stated above, if ER does not give consent, ETT will not have an access to the mine area it possesses since it is up to ER's own discretion whether to provide the consent. ETT's right to access to its own mine area as the license holder is restricted, thus this provision exceedingly serves for one-sided interest.

9.3 Under Article 8.2 (c) of the Cooperation Agreement, ER shall have a preemptive right to purchase the Tsankhi Mining License in case ETT decides to sell, transfer or otherwise dispose of such license to the third party in any way.

Moreover, under Article 8.2 (c) of the Cooperation Agreement, the purchase price [of the license] must be agreed and if the parties fail to agree on purchase price, the value will be determined by an internationally recognized professional independent valuation organization. Then ER will be entitled to purchase at the price determined by such organization. Although it is appropriate to have an independent international professional organization for valuation, it implies that ETT must sell the license only to ER at the determined value. This can be clearly seen from Articles 8.2 (b) and 8.2 (c) of the Cooperation Agreement which state that "it is prohibited to sell, assign, or otherwise dispose the Tsankhi Mining License to any third party without providing the Project Company with the preemptive right".

Also the sections (i) and (ii) of Article 8.2 (d) of the agreement restricts ETT to sell or transfer the mining license to any third party. For instance, aforementioned provisions state that **ETT shall provide ER with a copy of the written agreement executed by ETT and the transferee**; and the transferee **and ER** will execute

acknowledgement and accession deed, in the **substance and form of which must be as reasonably requested by ER**, according to which the transferee must agree to be bound by this agreement and the Investment Agreement. Such transaction will not be implemented only in the event ER intentionally proposes a deed with the terms and conditions that are not acceptable by the other party.

The Government must not agree to this kind of provisions that create such privileged right.

9.4 Article 5.1 (c) of the Cooperation Agreement and Article 2.3 (c) of the Investment Agreement provide the possibility of processing coal mined from Tsankhi mine area in combination of coals mined from other mines and produce products. The aforementioned "other mines" is understood as Ukhaa Khudag Deposit which is currently being used by ER.

Because Articles 1.1 (a), 5.2 (a) and 5.2 (e) of the Investment Agreement state that to develop the Tavantolgoi deposit **in connection with the operation of the Ukhaa Khudag Deposit**, both ETT and ER hold the mining licenses for Tsankhi Mine area and Ukhaa Khudag Deposit for 30 years subject to two times extension for 20 years each. Then, the total valid term of mining licenses will be 70 years. Accordingly, it is stated that the terms of this Investment Agreement will also apply to the activities of Ukhaa Khudag Deposit.

The scope of the Investment Agreement and other ancillary agreements must not involve any operation of Ukhaa Khudag Deposit and the Government and EET should not bear any obligation.

Since the Ukhaa Khudag deposit is not an subject of this Agreement, the provisions related to Ukhaa Khudag Deposit should be removed from this Agreement. Moreover, the Government did not make a decision to conclude the Investment Agreement with ER in relation with the Ukhaa Khudag Deposit.

9.5 Under Article 6.1 (l) of the Cooperation Agreement, **ETT has the obligation not to delay, disturb or disrupt implementation of the Project, the Mining Operation and other activities of ER**. This provision should be changed as to ETT would have the right to protect its interest granted by law in case ER violates, breaches the Agreement and/or laws.

9.6 Under Article 8.1 (a) of the Cooperation Agreement titled as "Assignment of rights and obligations", ER shall not transfer its rights and obligations under this Agreement to any third party, **without the prior written notice** to ETT.

However, Article 8.2 (a) of such Agreement states that "ETT shall not transfer, assign, or dispose any of its rights and obligations under this Agreement in whole or partially in any way to any third party **without the prior written consent** of ER".

Abovementioned provisions of the Agreement exceedingly serves for the interest of one side, which is ER, because ER is able transfer its rights and

obligations to a third party upon delivering a written notice to ETT while ETT should have obtained a written consent from ER in order to transfer, assign its rights and obligations to the third party. ER can limit ETT's right just by rejecting to issue a written consent. It would have been proper if the Parties of the Agreement were obliged under identical provisions. In other words, ER should not have the right to assign its rights and obligations to the third party without the written consent of ETT.

9.7 Under Article 14.8 of the Cooperation Agreement, Article 6 (Rights and obligations of ETT), Article 12 (Confidentiality of the Agreement), 13 (Power of Attorney) will survive notwithstanding the expiration or termination of this Agreement by any Party or for any reason,

Once the Agreement expires, the legal relationship between the Parties should be terminated, therefore, this provision is not acceptable. The Agreement should be terminated in whole save for the Confidentiality provision that can survive for a certain period.

9.8 Under Article 7.3 (e) of the Investment Agreement, ETT is not able to create any security interest, guarantee, warranty or assignment obligation over the Tsankhi Mining License, its related land rights in favour of a third party without prior written consent of ER. Furthermore, ETT may not transfer, assign, or otherwise dispose of in whole or in part of its rights and obligations under this Agreement to any third party, without prior written consent of ER under Article 14.2 of the Investment Agreement.

Moreover, it is stated in Article 8.1 (a) of the Cooperation Agreement that "ER shall not transfer its rights and obligations under this Agreement to any third party, **without prior written notice** to ETT".

Abovementioned provisions of the Investment Agreement do not satisfy the principle of equality, because ER is able transfer its rights and obligations to a third party upon delivering a written notice to ETT while ETT should have obtained a written consent from ER in order to transfer, assign its rights and obligations to the third party. ER can limit ETT's right just by rejecting to issue a written consent. It would have been proper if the Parties of the Agreement were obliged under identical provisions. In other words, ER should not have the right to assign its rights and obligations to the third party without the written consent of ETT.

9.9 Under Article 7.3 (f) of the Investment Agreement, ETT shall not participate or interfere in the business of ER, hinder, disturb or delay implementation of the Project, the Mining Operation and other activities of the Project, not make any decision or take any actions which may cause negative impacts on the Project implementation and Mining Operation and shall not impose any restrictions on the Project activities during the Term of this Agreement; and the Cooperation of the Parties are closed for 30 years

(with extension of another 30 years). (*The phrase "Any form" is removed from the draft Agreement as of 6 April 2015*)

This article is not acceptable because ETT would inevitably participate in the business of ER as the license holder to implement its rights and obligations provided in Article 27 titled "Rights and obligations of mining license holder" and the Chapter 6 titled "Obligations of a license holder" of the Minerals Law.

Moreover, many matters with business solutions may occur between these business partners during the 60 years of cooperation term of the Project. It is obvious that ER must cooperate with ETT for mutual business profitability since it will operate on the mining site possessed by ETT.

9.10 Under Articles 9.1 (a) and (b), ER together with all its affiliates "Energy Resources Mining" LLC, "Energy Resources Rail" LLC, "Enrostechnology" LLC, "United Power" LLC, "Ukhaa Khudag Water Supply" LLC, "Transgobi" LLC will be covered under tax stabilization.

ERC's subsidiaries and ER's affiliates that are operating on the Ukhaa Khudag Deposit should not be covered under the Investment Agreement for operating the Tavan Tolgoi because the operation of Ukhaa Khudag should be carried out separately. ER and its subsidiaries that possess the Ukhaa Khudag Deposit may submit a separate application for another Investment Agreement to stabilize the tax.

9.11 Under Article 22 (b) of the Investment Agreement, **only ER and Investors may propose to amend the Agreement** but ETT does not have such right. This intention is clearly confirmed by Article 7.2 (e) which states "During the Term of this Agreement, the Government … shall not impose any **additional conditions**". This provision exceedingly serves for the interest of one side by restricting the side of Mongolia to propose to amend and change the Agreement during the Term of such Agreement, which Term will be continued for 30 years with available extension of another 30 years. Therefore, the side of Mongolia should not accept this provision in any case.

9.12 Under Article 23.2 of the Investment Agreement, remedy period is 6 months for the Government while it is up to 2 years for ER and it violates the principle of equality because there is a drastic difference. Remedy period should be same for the Parties.

9.13 Under Article 21.1 (f) of the Investment Agreement, the **Government shall be jointly and severally liability for any action or omission of ETT and MTZ**.

The Government should not bear such liability because ETT and MTZ are entities that have a legal capacity according to the Civil Code and the Company Law and they must be severally liable for their action or omission.

In addition, "MTZ" company shall not have any future obligation since D.Ganbat, the Executive Director of MTZ, notified the Government and related high ranking state

officials in advance that “The MTZ does not agree to transfer the railway base structure in the direction of Ukhaa Khudag-Gashuun Sukhait to ERR because the transfer is illegal” by its official letter 01/281 dated 3 April 2015.

9.14 The Government of Mongolia, ETT and ER will be responsible for too many obligations toward the Project Financiers under the Investment Agreement. For example, see Articles 6.1(n), 7.1(h), (q), 8.4(c), (d) and 8.5 of the Investment Agreement.

Since the Project Financiers are not party to the Investment Agreement, the Government or ETT should not hold any obligations towards the Project Financiers.

The Financiers should enter into separate agreements for the financing of the project with ER, the Project Company, and the rights and obligations should arise of such agreements.

Any rights, obligations, and conditions in connection with the Project Financiers incorporated in the Investment Agreement and other related agreements are unacceptable and should be taken out from the agreements.

The Working Group on Tavantolgoi Project was supposed to carefully research the negotiation process and the contents of the Oyu Tolgoi Investment Agreement signed in 2009, learn from the mistakes made back then and keep those in mind while negotiating the terms of TT IA. As opposed to that, it appears that ALL similar disputed issues from OT project are drafted into the IA in favor of the Investors.

	OYU TOLGOI INVESTMENT AGREEMENT	**TAVAN TOLGOI INVESTMENT AGREEMENT**
1	**1.11** The Investor has the right to conduct the operations of mining and processing minerals from the underground mine area and the open pit mine area, and producing Products, within mining license 6709A of the Oyu Tolgoi Deposit. The reserves for these areas are registered in the national registry of reserves, and the Feasibility Study for these areas has been submitted to the State administrative authority in charge of geology and mining for its consideration in accordance with existing laws and regulations. Consideration of the Feasibility Study will be concluded in 150 (one hundred and fifty) days from the date of submission. **16.21 Feasibility Study** means a feasibility	**5.1(c)** The feasibility study may be subject to changes, revisions and amendments depending on results of the additional mining explorations within Tsankhi Coalfield and other activities of the Project conducted by Project Company pursuant to this Agreement, from time to time. In case of any material changes or adjustments are deemed necessary by Project Company for any feasibility study accepted by the Authority, Project Company shall submit to the originally accepting Authority such changes or adjustments, and the Authority shall issue a decision to accept and register such changes or adjustments promptly, latest within 150 (one hundred and fifty) days upon the submission, and/or if needed, according to the relevant Laws of Mongolia

	study for the proposed mining of reserves from the Contract Area, to be prepared in accordance with the requirements of the relevant Mongolian laws and regulations, or equivalent internationally recognized requirements, as updated from time to time.	(the "Feasibility Study"). **Comment: Major discrepancy between original English version and the Mongolian translation. The English version reads that the Authority <u>has to make a decision</u> to accept and register any revisions to the FS within 150 days and/or in accordance with relevant Laws of Mongolia(which is not well written at the moment). The Mongolian version implies that the Authority shall have the right to make a decision on whole FS issue in accordance with the laws of Mongolia. In addition, the Order 74 of the Minister for Minerals and Energy of 2012, which regulates how the relevant Authorities should approve the FS, is currently not registered with the Ministry of Justice making it unenforceable.**
2	**15.1 The Investor shall be entitled to assign its rights and obligations under this Agreement with the consent of the Government.**	**6.1(n)** Project Company shall have the right to change or assign by way of security in its rights and benefits under this Agreement in favor of the Financiers; **8.3(b)** Investors and Project Company shall have the right to create a security interest in its rights and benefits of this Agreement, the Products produced from Tsankhi Coalfield and the coal processing plant, water and power supply infrastructures, other facilities, constructions and other properties, rights and interests associated with the Project under this Agreement, in order to obtain financing in relation to the Project; **8.4(d)** The Government, if necessary, together with other Authorities shall enter a direct agreement (hereinafter referred to as the "Direct Agreement") at the request of Financiers including Project Company. The Direct Agreement shall include following terms and conditions: (i) In case when Project Company fails to perform its obligations under this Agreement, the Financiers shall be notified in reasonable time and the Financiers shall

		be entitled a reasonable time period to step-in to the Project and remedy the default; **Comment: It is clear from the draft IA that the Project Company will create a security interest in its rights and benefits in the future and the GOM will be forced to enter into Direct Agreement with the Financiers, the terms of which are unknown. The question should be asked whether this is acceptable from the GOM's point of view.**
3	**9.10** The Investor has the following rights: **9.10.3** to retain abroad and freely dispose all of its proceeds received outside of Mongolia from the export, sale or exchange of Product; **9.10.4** to freely repatriate abroad without any barriers and to and freely dispose of, all proceeds (including by way of dividend or other form of distribution) received within Mongolia from the sale, exchange or export of Product, and any other payments (including loan principal and interest) to be made abroad;	**3.7(c)** Project Company shall be entitled to maintain bank accounts in a commercial bank of Mongolia and elsewhere, and Project Company may make international transactions freely and without any obstructions in its chosen currency, including: (ii) to hold any funds inside or outside of Mongolia and freely transfer and dispose of such funds after fulfilment of its tax payment obligation; (iii) to retain in Mongolia or abroad and freely dispose of its proceeds received outside of Mongolia from the export, sale or exchange of Products; (iv) to freely repatriate in Mongolia or abroad and freely dispose of proceeds (including by way of dividend or other form of distribution) received within Mongolia from the sale, exchange or export of Products, and any other payments (including loan principal and interest) to be made abroad; **Comment: The Investor is not obliged to maintain any portion of its proceeds from the sale of products in Mongolia. Almost every politician in Mongolia complains about how at least certain portion of the proceeds from the sale of OT products are not maintained in the country, thereby having no impact on domestic MNT/USD exchange rates. Are**

		we all on the path to make same mistake? It should be noted that early in 2015, the GOM and Mongolbank jointly approached and requested OT to keep proceeds from the gold portion of the Project in Mongolia and the proposal was rejected.
4	**9.6** The development of the OT Project may occur in stages as determined by the Investor as reflected in the Feasibility Study, taking into account market conditions and financing issues (including availability and terms of finance for the OT Project). If the Investor materially changes its proposed sequence for the development of the OT Project, the Investor shall inform the State administrative authority in charge of geology and mining in writing of such change.	**4.2(b)** The development of the Project may be implemented in stages as determined by the Project Company, taking into account market conditions and financing issues (including availability and terms of financing for the Project). If Project Company materially changes its proposed sequence for the development of the Project, Project Company shall inform the Government in writing of such change. **Comment: The English version is almost exactly the same as the Clause 9.6 of the OT Investment Agreement. This is a Clause that the Investors in OT project always refer to when the GOM representatives raise an argument about the "stages" of the Project, and the financing of every "stage" as wells as security interests related to those financing methods.**
5	**9.5** The Investor has invested a significant amount of capital in exploring and developing the OT Project, through the financial capability of Ivanhoe Mines Ltd and Rio Tinto, pursuant to the Existing Shareholder Loans. The Investor plans to make an additional investment in the OT Project, the estimated amount of which, as provided in the Feasibility Study referred to in Clause **Error: Reference source not found**, will be approximately USD4 Billion. The estimated initial capital will be invested over a period of 5 (five) years, and a schedule for this planned expenditure is contained in the Feasibility Study.	**2.8(a)** The preliminary estimate of the total investment by the Project Company for this Project is approximately USD 4 (four) billion. **Comment: A lesson needs to be learnt here from OT's example, in which the initial investment of USD 4 billion is defined in "approximate" terms that has significantly increased later on and led to large cost overruns. Unarguably, the cost overruns of OT project had a direct negative impact to the benefits supposed to be received by Mongolia;**
6	**3.13** The Investor shall pay a royalty under Article 47.3.2 of the Minerals Law at the date of this Agreement equal to 5% (five	**9.2(r)** In accordance with the Clause 9.2(a) of this Agreement, the Parties agreed to stabilize Royalty rates during the

	percent) of the sales value of all Products mined from the Contract Area that are sold, shipped for sale, or used by the Investor, and such royalty is Stabilized.	Stabilization Period as in force on the Effective Date at following rate: (ii) base Royalties for extracted coals that are exported shall be five (5.0) percent of the sales value of all products extracted from the mining claim that are sold, shipped for sale, or used as per Article 47.3.2 of the Minerals Law of Mongoia; **Comment: A risk of tax dispute in the future resulting from differences in defining the sales value of the products exported to the markets other than PRC market and how to calculate the overall amounts in sales contracts.**
7	**2.2** Tax to be withheld as a result of the Corporate Income Tax Law shall be calculated at the rates specified in the respective clauses of the Corporate Income Tax Law (as in force on the date of this Agreement), which includes in accordance with any applicable double tax treaties as applied by Article 2.2 of the General Taxation Law, and which rates shall be Stabilized.	**9.2(c)** Tax to be withheld as a result of the Law of Mongolia on Corporate Income Tax shall be calculated at the rates specified in the respective provisions of the Law of Mongolia on Corporate Income Tax (as in force on the Effective Date), and any applicable tax treaties to avoid double taxation as allowed by Article 2.2 of the General Taxation Law of Mongolia, and which rates shall be Stabilized. For avoidance of doubt this Clause shall apply only to withholding tax on loan interest to be paid by the Project Company to creditors and shareholders and dividend on common or preferred shares to be paid to shareholders; **Comment: Needs to clarify why other taxable incomes listed in Clause 17.2.9 of the Law on Corporate Income Tax are excluded here. Only loan interests and dividends are mentioned.**
8	2.12. In accordance with Government Resolution Number 287 approving a procedure on carrying tax loss forward in mining and infrastructure dated 16 September 2009 made under the authority of the Corporate Income Tax Law, the tax loss of the Investor to be determined in accordance with Articles 20.1 and 20.2 of the Corporate Income Tax Law shall be carried forward and deducted from the taxable income of the Investor in the next 8	2.2(d) The exploration costs incurred for additional exploration work of the Project Company shall be deductible from the taxable income of the Project Company as provided in Clause 9.2(I) of this Agreement; 9.2(i) During the Stabilization Period, the tax loss of the Stabilized Entities shall be determined in accordance with Articles 20.1 and 20.2 of the Law of Mongolia on

	(eight) consecutive years after the tax year in which such tax loss was incurred. This will not apply for losses specified in tax statements for the tax year occurring before 1 January 2007. Tax losses of the Investor specified in the tax statements of that tax year occurring during the period from 1 January 2007 to 31 December 2009 (inclusive) shall be carried forward and deducted from the Investor's taxable income in the next 2 (two) consecutive years after the tax year in which such tax loss was incurred and the amount of loss to be deducted annually shall not exceed 50% (fifty percent) of the Investor's taxable income for that year. However, tax losses of the Investor specified in tax statements for each tax year occurring from 1 January 2010 shall be carried forward and deducted from the Investor's taxable income in the next 8 (eight) consecutive years after the tax year in which such tax loss was incurred and the amount of loss to be deducted annually shall not exceed 100% (one hundred percent) of the Investor's taxable income for that year.	Corporate Income Tax and Government resolution No.287, 2009 shall be carried forward and deducted from the taxable income of the Stabilized Entities in the following 8 (eight) consecutive years after the tax year in which such tax loss was incurred; **Comment: A risk of tax dispute if the Project Company faces significant cost overruns and that affects the amount of taxes paid to the GOM. OT is a classic example of this.**
9	The Parties agree that in respect of the financing of the OT Project: The Investor shall deliver to the Government a notice informing that the Financing Completion Date has occurred within 7 (seven) days of such date being achieved; the Investor shall achieve Commencement of Production within 5 (five) years of the Financing Completion Date; and 3.10.3 the "**Financing Completion Date**" referred to in this Clause The Parties agree that in respect of the financing of the OT Project: is the date being the earlier of: 3.10.3.1 the date on which the Investor has managed to secure (or have made available to it) sufficient financing facilities on terms, including in respect of guarantees, security or other support,	**12.4(a)** Project Company plans to market and sell 75% of the total Products to the PRC market, and the remaining 25%, through the Trading JV, to Japan, Republic of Korea, India and other countries and regions, provided that the actual sales volume of the Products will depend on many factors including availability of railway transit transportation, market conditions and prices; **Comment: Time again, the important matters for Mongolia is defined in very vague terms and the liabilities of the Investors are not very clear in case there is a violation of this Clause.**

	reasonably acceptable to the Investor, to enable the full and complete construction of the OT Project as described in the Feasibility Study referred to in Clause The Investor has the right to conduct the operations of mining and processing minerals from the underground mine area and the open pit mine area, and producing Products, within mining license 6709A of the Oyu Tolgoi Deposit. The reserves for these areas are registered in the national registry of reserves, and the Feasibility Study for these areas has been submitted to the State administrative authority in charge of geology and mining for its consideration in accordance with existing laws and regulations. Consideration of the Feasibility Study will be concluded in 150 (one hundred and fifty) days from the date of submission., and notified to the Government in writing; and 3.10.3.2 2 (two) years after the Effective Date.	
10	If a dispute is not settled by negotiation in accordance with Clause Error: Reference source not found, it shall be resolved by binding arbitration in accordance with the procedures under the Arbitration Rules of the United Nations Commission on International Trade Law (the "UNCITRAL Rules") as in force at the time of the dispute. Accordingly, the following shall apply: 14.2.1 the number of arbitrators shall be 3 (three); 14.2.2 the 3 (three) arbitrators shall be appointed in accordance with rules 7 and 8 of the UNCITRAL Rules; 14.2.3 the language of the arbitration shall be English; 14.2.4 the arbitrators shall apply the laws and regulations of Mongolia to the interpretation of the Investment Agreement; 14.2.5 the place of arbitration shall be in	26.1(d) Arbitration: (i) If, notwithstanding such meeting between senior representatives of the Parties pursuant to Clause 26.1(b) the Parties are unable to resolve the dispute within sixty (60) days of service of the Dispute Notice, then any Party shall be entitled to refer the dispute to arbitration. For avoidance of doubt, it is not necessary for the Parties to refer the dispute to Expert before arbitration; (ii) Parties hereby consent to submit to the International Center for Settlement of Investment Disputes (the “ICSID”) any Dispute for settlement by arbitration pursuant to the Convention on the Settlement of Investment Disputes between States and Nationals of Other States (the “ICSID Convention”) (iii) The number of arbitrators shall be 3 (three), the Government shall appoint 1 (one) arbitrator, and Project Company shall appoint 1 (one) arbitrator and chairman of

	London, United Kingdom; and 14.2.6 the arbitral proceedings shall be administered under the UNCITRAL Rules by the London Court of International Arbitration.	the ICSID shall appoint 1 (one) arbitrator who shall be the chairman of the arbitration tribunal; (iv) The language of the arbitration shall be English; (v) The arbitral award shall be final and binding on the Parties, and judgment on the award may be entered by any court having competent jurisdiction; (vi) The place of Arbitration shall be London; (vii) The Parties hereby commits to approve fully and implement the execution and enforcement of the arbitral award; (e) The dispute resolution procedure provided under this Clause shall be effective, irrespective whether the Agreement stays in force; **Comment: The underlying question we should ask is that: in case if the Project Company materially violates the Investment Agreement, does the Government of Mongolia have resources, capacity, and will to start arbitration proceedings in London? How would such arbitration impact our bilateral relations with neighboring countries and how should we measure political risk out of it? Moody's report clearly indicates that China Shenhua Energy, the Foreign Investor of this Agreement, is 73% owned by PRC's state controlled Shenhua Group.**

The Working Group concludes that the terms and conditions of the Investment Agreement, the Cooperation Agreement, and the Railway Concession Agreement for the operation of the Tavantolgoi Coal Deposit, to be signed with the Consortium, are too unfair, one-sided, and are clearly in favor of the Investor, and the agreements also limit the rights of the Government and the state owned Erdenes Tavantolgoi JSC.

Ten. Evaluation of economic profitability from agreement and its positive and negative effects

10.1 It is not possible to pre-determine the economic profitability of Tavan Tolgoi Coal Deposit operation on the basis of the Investment Agreement and related agreements as the Consortium proposed.

Because, Article 2.1 (c) and (d) of the Investment Agreement states that "ER has right to determine detailed mining plan, development programmes, costs of mining operation and constructions and investment terms and authorize to make all decisions and take all actions related to Mining Operation and other activities of the Project including without limitation conducting the study, calculation, mine development and exploration planning, defining the scope of the Mining Operation and reporting actions independently in its own discretion".

Further, the ER "has right to renew the existing feasibility studies prepared by the ETT and develop a new feasibility study for the Mining Operation; to make revision and amendments to the feasibility study and determine detailed mining plan, development programmes, costs of the Mining Operation and constructions and investment terms and conditions; and to export and sell the Products produced and mined coals, undertake all activities related with the coal sale, such as storage, loading, reloading, stockpiling, transportation and logistics, handling, customs clearance and export, trading and marketing on its own, collect and spend coal sale revenues". (*Article 5.1 (b) of the Investment Agreement and 5.1 (d) and (n) of the Cooperation Agreement*)

Moreover, the ER is "entitled to independently determine the actual quantity of Products to be mined and processed from Tsankhi Coalfield in any year, to work independently and make decisions with respect of the sale of Products on its own, such as, defining markets for the product sale, defining coal processing costs and rates, defining volume and price of Products and defining the frequency of the shipments and transportation engagements and other commercial terms". (Articles 2.4 (b) and 2.b (b) of the Investment Agreement)

Under Articles 2.8 (b), 4.3 (a, c) and 5.1 (b), (c), "above [investment] figures are only indicative and shall be determined based on the Feasibility Study developed and revised by the ETT from time to time and shall be subject to further changes depending on the market conditions; and ER shall determine the schedule for investment based on the Feasibility Study and Financing Agreements entered with the Financiers, and shall have the right to make any adjustment or changes to the schedules pursuant to the operation needs of the ER and then-current market conditions so long such change is permitted under the Financing Agreements. The ER shall renew the existing feasibility study for the Mining Operation within twelve months, and renew the existing feasibility studies prepared by the ETT and develop a new feasibility study for the Mining Operation; the feasibility study may be subject to changes, revisions and amendments depending on results of the additional mining explorations".

Therefore, all the economic profitability cannot be pre-determined from the Investment Agreement and related agreements, save for certain payments such as the Prepayment (200 million USD) to be paid upon conclusion of the Agreement, payment for development of the Railway base structure in the direction of Ukhaa Khudag – Gashuun Sukhait (192. 226. 432 USD), and Chalco debt payment (142 million USD).

In case ER independently determines the amount of coal to be mined and processed depending on the market conditions, there is a risk that amount of tax payable to the Government and cooperation payment payable to ETT may decrease.

10.2 In consideration of ER's promotion about economic profits

ER has been announcing to public that the Agreement will directly bring 620 million USD of in cash as soon as it is concluded and it is expected to be real profit for Mongolia. However, articles of the Investment Agreement is not consistent with this public announcement.

Announcement of the "Energy Resources"	**Statement in the Investment Agreement**
Prepayment of 200 million USD will be paid. (as soon as the Agreement is signed)	**3.3 Prepayment** (a) Project Company shall make a total of USD 200 (two hundred) million prepayment to the Government and ETT (the "**Prepayment**") within [10] calendar days **upon the fulfilment of all the conditions precedent set out in Clause 3.3(d)** (the "**Prepayment Date**"); (b) The Prepayment shall be recouped fully by deducting from and setting off against (i)Project Company's obligation to make payment of the future Taxes payable to the Government and/or (ii) the Cooperation payment payable to ETT under Clause 3.1 of this Agreement (item (i) and (ii) together, the "**Deductible Amount**"). The Project Company shall enter into a separate Prepayment agreement to regulate detailed terms and conditions regarding the Deductible Amount with Government and ETT respectively. (c) The Parties agree that interests shall accrue at the rate of [4.5%] (the "**Interest**") per annum on any outstanding amount of the Prepayment after deduction of the Deductible Amount from the total amount of the Prepayment.
140 million USD of Chalco debt will be paid. (as soon as the Agreement is signed)	3.4 Settlement of existing assets and liabilities of ETT (a) The Project company shall independently

	decide to pay on behalf of ETT an amount equivalent to the outstanding debts in the amount of USD [142 (one hundred forty two) million] together with accrued interest, if applicable, (the "**Chalco Debt**") arising out of the Coal Sale and Purchase Agreement entered into between ETT and Chalco Trading (Hong Kong) Company of PRC dated 2011 (the "**Chalco Agreement**"), **either way of supplying Products or in cash the payment methods shall be determined in the Settlement Deed**. The Chalco Debt shall be paid fully within 12 months starting from the Prepayment Date. ETT shall be obligated immediately to transfer to Chalco any cash payment or any coal supplied by the Project Company to ETT in order to repay Chalco Debt in accordance with procedure agreed in the Settlement Deed, and the Project Company shall not be responsible for any interest fee, penalties, costs, losses, damages and claims incurred due to delay of payment by ETT to Chalco. The Project Company shall hold ETT harmless from and against any and all losses, costs and claims that ETT suffers or incurs as a result of, arising from the Project Company's delayed payment of the Chalco Debt. The Chalco Agreement shall not be assigned or transferred to the Project Company and ETT and Chalco shall remain to be the Parties to the Chalco Agreement. After full payment of Chalco Debt, the Project Company with support of ETT shall develop suitable solutions to resolve continuing coal supply obligation of ETT under the Chalco Agreement. (b) ETT shall solely be liable for any debts other than those specified in Clause 3.4(a) of this Agreement, which arise before the execution of the Transfer and Novation Agreement.
	"MTZ" JSC spent 196.709.432 milion USD for the railway base structure in the direction of Ukhaa khudag- Gashuun Sukhait. 22.517.00 million USD was paid for the railway structure drawings and consultation fee. Energy Resources company spent 93.6 billion

280 USD will be reimbursed for the railway work. (as soon as the Agreement is signed)	togrog on the construction of the railway in the direction of Ukhaa Khudag – Gashuun Sukhait. (Above figures were accepted by the Conclusion of workgroup organized jointly by Minister of Economic development, Minister of Finance, and Minister of Road and transportation; and it will be included in the returnable asset which is dedicated to be converted into company shares for the purpose of the Project) Total amount is: 192,226,432 USD and 93,6 billion togrog. Under the 3.5(a) of the Investment Agreement, subject ot the Railway Concession Agreement, Concessionaire will reimburse the actual costs incurred by Government for the Ukhaa Khudag – Gashuun Sukhait Railway Project based on the technical, financial and legal due diligence carried out by the Consortium;[7] Payment will be paid upon fulfillment of 6 conditions precedents stated in the 3.5(b) of the Investment Agreement. Payment made by Government will not be returned as soon as the Agreement is signed.

[7] Terms as stated in Article 3.5(b), 1. This Agreement, the Cooperation Agreement and the Railway Concession Agreement have been duly executed by the parties thereto and became effective; 2. Concessionaire has received the License to Build the Railway; 3. Consortium have completed its due diligence regarding Ukhaa Khudag-Gashuun Sukhait Railway Project; 4. Based on result of the due diligence, Concessionaire and MTZ have executed a project transfer agreement (the "**Project Transfer Agreement**") and completed all transfers and novation through signing of transfer act as per the Project Transfer Agreement; 5. The Government has approved the Railway alignment for railway base structure to be constructed under the Railway Concession; 6. The Government has issued the Permits for the Land Strip (as defined in the Railway Concession Agreement) in accordance with the Railway Concession Agreement under the relevant Laws of Mongolia.

Conditions precedent for making the Prepayment shall include the following: 1. This Agreement, the Cooperation Agreement, and the Railway Concession Agreement have been duly executed by the parties thereto and become effective; 2. Concessionaire has received the License to Build the Railway; 3. The Project Company has entered into a Prepayment agreement with the Ministry of Finance and ETT in relation to the Prepayment under Clause 3.3 of this Agreement; 4. Project Company has completed its technical, financial and legal due diligence regarding ETT's existing assets related to the Tsankhi Coalfield mining production, operation, sales and transportation, and existing contracts related to the Tsankhi Coalfield mining and coal sales and employees; 5. Based on result of the due diligence, Project Company and ETT have executed the Transfer and Novation Agreement and completed all transfers and novation through signing of transfer act as per the Transfer and Novation Agreement. 6. Settlement deed related to the Chalco Debt has been executed between the Project Company and ETT pursuant to Clause 3.4(a) of this Agreement (the "**Settlement Deed**"); 7. ETT has fully transferred TT Land to possession of Project Company; and 8. All the Conditions set out in Clause 4.1*(d) have been fulfilled.

The Agreement provides that the USD 142 million debt to China's Chalco may be repaid with coal; thus, it is unlikely that the repayment will be in made in cash immediately upon the execution of the Agreement.

Article 3.3(a) of the Investment Agreement states that the prepayment to the Government and ETT (the "**Prepayment**") shall be made within [10] calendar days **upon the fulfilment of all the conditions precedent set out in Clause 3.3(d)** (the "**Prepayment Date**"); thus, the USD 200 million prepayment will not be transferred **as soon as** the Agreement is signed.

Moreover, the USD 192,226,432, which the Government has invested in the Ukhaa khudag-Gashuun Sukhait railway, will not be repaid until the 6 different conditions precedents of Article 3.5(b) of the Investment Agreement are fulfilled.

10.3 Regarding the steady annual income mentioned in ER's advertisement:

Export income 1.2 billion (will lead to expansion of foreign currency flow and stabilize domestic currency)	Article 3.7(c)(iii) of the Investment Agreement states that income derived in Mongolia from exports, sales, and trade (including dividends) shall be freely deposited within or outside of Mongolia, be disposed of, and be transacted outside of Mongolia. Article 3.7(c)(iv) of the Investment Agreement states that income derived outside of Mongolia from sale, trade, and export shall be freely deposited within or outside of Mongolia and be disposed of. As above articles states, it is not clear what percentage of the proceeds from the export of the Product will be deposited in Mongolia or abroad. Therefore, ER can deposit all of such proceeds; otherwise, it can deposit most of such proceeds in foreign country by leaving very small portion in Mongolia. Please see the conclusion of this part from 10.5 of this Workgroup conclusion titled as Income.
Investments equaling USD 5 billion will be made within the first 5 years	Articles 2.8 (b), 4.3 (a, c) and 5.1 (b), (c) of the Investment Agreement provides that the investment amounts are only indicative and shall be determined based on the Feasibility Study developed and revised by the ETT from time to time and shall be subject to further changes depending on the market conditions; and ER shall determine the schedule for investment

	based on the Feasibility Study and Financing Agreements entered with the Financiers, and shall have the right to make any adjustment or changes to the schedules pursuant to the operation needs of the ER and then-current market conditions so long such change is permitted under the Financing Agreements. ER shall renew the existing feasibility study for the Mining Operation within twelve months, and renew the existing feasibility studies prepared by the ETT and develop a new feasibility study for the Mining Operation; the feasibility study may be subject to changes, revisions and amendments depending on results of the additional mining explorations. Moreover, Pre-stripping is stated as investment in the 2.8(a)(iii) of the Investment Agreement. Pre-stripping is not an investment but an operational cost incurred during the mining process. If costs like this are included in the investment, ER, within very short period, can report that it has performed its investment obligation. In other words, ER is trying to be freed from its real investment obligation by marking its operational cost as investments. Please see the conclusion of this part from 10.6 of this Workgroup conclusion titled as Investment.

We consider that ETT's income from this project is too low. At present, when market conditions are at its worst, ETT was still able to sell 5.8 million tons of raw coal, and it had an income of 400 billion togrogs, of which 28 billion was in profits. Taking into account the highest possible income for ETT as stated in the Cooperation Agreement, which calculates to USD 30 million, ETT will be unable to perform its obligations before its banks and operators.

10.4 Economic analysis of the Tavantolgoi project

The Working Group has laid out three potential developmental scenarios and their respective economic benefits for the Tavantolgoi project. Please note this is a preliminary analysis and subject to change.

This preliminary economic analysis was based on the technical assumptions specified in the feasibility study, which was prepared by GLOGEX and submitted to ETT (the "GLOGEX feasibility study"), as well as MMC's annual reports from the last three financial years.

Technical Assumptions:

- The GLOGEX feasibility study assumes ROM production of 882.8 mt and processing of 614.2 mt of coal over the project's term of 30 years, from West Tsankhi, East Tsankhi and Ukhaa Khudag.
- As there was no clear breakdown of coal production between the Tsankhi and Ukhaa Khudag basins, we assumed the Ukhaa Khudag production volumes to be equivalent to those of MMC's 2014 operations.
- The prices assumed in the GLOGEX feasibility study, of hard coking coal (HCC), semi-soft coking coal (SSCC), thermal coal and middlings were used as is.
- In addition, cost of goods sold ("COGS") and selling, general & administrative ("SG&A") expenses were assumed to be in line with the GLOGEX feasibility study.

Financial Outputs:

- At the weighted average cost of capital ("WACC") of 14.1%, the project NPV is estimated to be US$47 million and IRR to be 14.7%.
- In calculating the WACC, we assumed the cost of equity of 25% and cost of debt of 6.8% on a debt-to-equity ratio of 60:40.
- Out of the proposed US$4 billion investment to be made by the investors, US$1 billion is an amount that has already been invested into the Ukhaa Khudag basin operated by Energy Resources LLC and the remaining US$3 billion is an actual cash inflow, as specified in the GLOGEX feasibility study.

Discount Rate	Net Present Value (NPV) (US$ million)
10.0%	467
12.5%	183
15.0%	(22)
17.5%	(170)
20.0%	(278)

Scenario 1. The Consortium of MMC and Shenhua to 100% co-own the project

- This scenario creates a total project cash flow of US$15.6 billion over the course of 30 years.

- Out of which, US$5.4 billion will be paid to the Government of Mongolia in forms of, without limitation, royalty taxes, income taxes, customs fees and dividend taxes.
- The Consortium members, namely MMC and Shenhua, will receive US$ 10.1 billion in forms of dividend, accumulated cash and cash equivalents, and profits to be earned by the subsidiaries involved in the project as subcontractors.
- Cash flow per each Mongolian citizen will be US$1,817, assuming population of 3 million people.

Scenario 2. State owned enterprise Erdenes Tavantolgoi JSC to own 51% of the project and a consortium of domestic and international investors to own 49% of the project

- In the Scenario 2 where ETT owns 51% and a consortium of domestic and international investors owns 49% of the project, the project will generate a total of US$13.5 billion worth of cash flow over the project term of 30 years.
- Out of which, US$9.6 billion will be paid to the Government of Mongolia in forms of, without limitation, royalty taxes, income taxes, customs fees and dividend taxes.
- Investors owning 49% of the project will receive US$3.9 billion in forms of dividend and accumulated cash and cash equivalents.
- Cash flow per each Mongolian citizen will be US$3,186, assuming population of 3 million people.

Scenario 3. State owned enterprise Erdenes Tavantolgoi JSC to remain 100% owner of the project

- In the Scenario 3, where ETT is expected to operate the project on a sole basis, the project will generate a total of US$13.2 billion.
- Cash flow per each Mongolian citizen will be US$4,396, assuming population of 3 million people.

The table below exhibits a more detailed breakdown of the economic analysis.

Analysis of

In US$ million

10.5 Revenue and Proceeds from Tavantolgoi project

It is stated in Article 3.7 (c) (ii) (iii) (iv) and 6.1 (f) of the Investment and Cooperation Agreement dated on April 6, 2015 that ER may make **international transactions freely and without barriers in its chosen currency, hold and freely dispose of any funds of Mongolia, and retain abroad and freely dispose all of its proceeds received outside of Mongolia.** Following changes have been made to the amended version of Investment and Cooperation Agreement submitted to Parliament by the GoM on April 23, 2015:

- "To hold and freely dispose of any funds both within Mongolia and outside of Mongolia after fulfilling tax requirements" in Article 3.7 (c) (ii) of the Investment and Cooperation Agreement
- "to retain and freely dispose (by way of dividend distribution) all of its proceeds received both within Mongolia and outside of Mongolia from the export, sale or exchange of Product" in Article 3.7 (c) (iii) of the Investment and Cooperation Agreement
- "to freely repatriate and freely dispose of all proceeds received within Mongolia from the sale, exchange or export of Product and any other payments within Mongolia and abroad "Article 3.7 (c) (iv) of the Investment and Cooperation Agreement

Even though "Mongolia" has been added to the Articles of the Investment and Cooperation Agreement, ER's right to retain all of its proceeds outside of Mongolia remains. Main principle has not been changed. Proceeds can either be retained within Mongolia or outside of Mongolia. Therefore, in accordance with this Article, the contract will not be breached if ER retains all of its proceeds from operations of TT or retain 1% of total proceed within Mongolia and 99% of total proceeds outside Mongolia.

It remains uncertain that abovementioned Articles of Investment and Cooperation Agreement will have impact on increasing the foreign exchange reserve of Mongolia and stabilizing the Mongolian tugrik.

10.6 Regarding the Investment

The preliminary estimate of the total investment by the Project is **approximately USD 4 billion** as stated in Article 2.8 (a) Investment Agreement and such amount is inclusive of the **investment that have been made to the Ukhaa Khudag Coalfield by ER.**

ER calculated that its investment made to the Ukhaa Khudag deposit is USD 1 billion. Minister M.Enkhsaikhan's letter numbered ZG-3/54 and dated 26 January 2015 in response to the enquiries of the Democratic Party caucus, stated "… the Consortium proposed to invest USD 4 billion in the Project; of that amount, **USD 1 billion will be invested through the in-kind contribution of Energy Resources LLC's Ukhaa Khudag industrial complex** and the remaining USD 3 billion will be contributed in cash.

As stated in Article 2.8 (a) Investment Agreement, the investment consists of the following 8 main components:

1. Railway project;
2. Mining equipment;
3. Pre-stripping;
4. Coal handling and processing plant;
5. Water supply facilities;
6. Power supply;
7. Construction of support facilities and infrastructure;
8. Other.

As the Minister M.Enkhsaikhan reports, **mining equipment, coal handling and processing plant, water supply facilities, and power supply** from above components are ER's assets that are being utilized at Ukhaa Khudag Coalfield at present.

However, there are no Articles or provisions in the Investment Agreement identifying the amount of investment made to Ukhaa Khudag and methods, formulas to calculate such amount. MMC is ER's parent company and owner. MMC's total debt is 1.285 billion including its long and short term debts as of 31 December 2014. It is shown in the MMC's financial statement for the period ended 2014 (page number 14 and notes number 23, 25, 26).

MMC's total debt of USD 1,285,987,000 includes short-term debt of USD 413,012,000 and long-term debt of USD 872,975,000. (Source of information: page 14 of the MMC's financial statement for the period ended 2014)

From its long-term debts, USD 114,818,000 should be paid within a year while USD 166,818,000 should be paid 1-2 years (Source of information: page 169 of the MMC's financial statement for the period ended 2014). MMC's short-term debt is USD 298,118,000. The aforementioned debts will become payable on the day of the invoice or within 2 months from the invoiced day (Source of information: page 170 of the MMC's financial statement for the period ended 2014).

Furthermore, "KPMG" auditing company stated in MMC's financial statement for the first half of 2014 that MMC will be unable to conduct its regular business operations (page 59). MMC's owner's equity was USD 396.5 million as of the end of 2014 while it was 560.9 million in the end of 2013, so there was 29.9% year to year decrease (page 14).

MMC's total debt is USD 1.17 billion as of 3 May 2015.

MMC paid a high price to purchase the Baruun Naran coal deposit in Tsogtsetsii soum of Umnugovi province, which led to MMC's increase of debts. "Kerry Mining" (Mongolia) Company paid USD 269 million for this coal deposit in 2008 and sold it to MMC for USD 464 million in 2011. However, the value of this coal deposit has decreased to 190 million in 2014. (Please see detail explanation about this acquisition from 10.9 of this Workgroup conclusion)

Moreover, the **mining equipment, coal handling and processing plants, water supply facilities, and power supply** facilities are marked as investment, but all these are pledged as security for a USD 570 million of loan issued from specific international bank. The Agreement must consider and provide how such debt and security interest will influence the investment. (Source of information: *http:upload.mmc.mn/financial report/* audit report of the KPMG auditing company, page 59)

The amount of investment by the investor should be the key metric for the Investment Agreement. However, Investment Agreement only provides an approximate estimate for the amount of investment; furthermore, the investment's timing and methods are left to the Investor's discretion.

ER has no obligation to invest exactly USD 4 billion since Article 2.8(a) of the Investment Agreement states "… **approximately 4 billion**" and Minister M.Enkhsaikhan's official letter states "**up to 3** billion USD of investment will be made".

The Agreement lacks any figures and timings as to exactly what the amount of investment obligations of ERC and Shenhua are as investors in ER.

Under Articles 2.8 (b), 4.3 (a, c) and 5.1 (b), (c), "**above [investment] figures are only indicative and shall be determined based on the Feasibility Study developed and revised by the ETT from time to time and shall be subject to further changes depending on the market conditions; and ER shall determine the schedule for investment based on the Feasibility Study and Financing Agreements entered with the Financiers, and shall have the right to make any adjustment or changes to the schedules pursuant to the operation needs of ER and then-current market conditions so long such change is permitted under the Financing Agreements. ER shall renew the existing feasibility study for the Mining Operation within twelve months of the execution of the Agreement, and renew the existing feasibility studies prepared by the ETT and develop a new feasibility study for the Mining Operation; the feasibility study may be subject to changes, revisions and amendments depending on results of the additional mining explorations**".

Under Articles 4.2(a), 4.3 (a) and (c), stages to implement the Project and schedule for the Investment shall be determined by ER itself and ER shall have right to make any adjustment or changes to schedule for the Investment. According to these articles, ER has the discretion to decide when and how to invest, and ER's obligation is to only inform the Government in writing of such changes.

Moreover, Pre-stripping is stated as investment in the 2.8(a)(iii) of the Investment Agreement. Pre-stripping is not an investment but an operational cost incurred during the mining process. If costs like this are included in the investment, ER, within a very short period, can report that it has performed its investment obligation. In other words, ER is trying to be freed from its real investment obligation by showing its operational cost as the investment.

In addition, ER may show large amount of exploration expense and will obtain right to extend term of Agreement for the purpose to recover such exploration expense. Because, under Article 2.2(a), ER will conduct **additional exploration** on the Tsankhi Coalfield area with a view of increasing reserves; and under Article 4.1(f), **Parties shall mutually resolve whether to extend the term until the full repayment of investment injected by ER into any exploration work**. (*In the draft of 6 April 2015, it was stated as "this article will be the ground for ER to have right to extend this Agreement until it fully recovers its investment injected to the exploration work" but in this draft it is mitigated it as "Parties shall mutually resolve"*)

This Article of the Agreement conflicts with Article 2.2(d) which states, "**the exploration costs incurred for additional exploration work of ER shall be deductible from the taxable income of ER as provided in Clause 9.2(i) of this Agreement**".

Since, under 2.2(d) ER is deducting its explorations costs from taxable income, it will not incur any losses. Thus, there should be no issue about recuperating all of its exploration costs between the parties and any extension of the Agreement's term is moot.

Considering above mentioned Articles of the Investment Agreement, it is not clear when and how ER will make the USD 4 billion in investments and how to determine if the investment is made. The Investment Agreement allows ER to split the approximately USD 4 billion and invest it for 60 years which includes the Term of the Agreement 30 years and additional 30 years of extension; it allows ER reinvest its income derived from the operation of the Tavan Togloi Deposit; or it allows ER to decide the method of investment on its own discretion such as by calculating adding high operations expenses like pre-stripping costs as investments.

In this Agreement, the Government has no demand rights with regards to the investment.

Article 8.1(a) of the Investment Agreement provides that ER may source the required funds to implement the Tavan Tolgoi Project through either selling shares or debt financing whichever ER deems more appropriate.

ER has the right to create security interests over its rights and benefits provided under this Agreement, the Products produced from Tsankhi deposit and the coal processing plant, water and power supply infrastructures, other facilities, constructions and other properties, all other rights and interests associated with the Project under this Agreement, in order to obtain financing for the Project. (Article 8.3(b) of the Investment Agreement)

ER is able to raise investment only by way of creating security interests over its rights and benefits obtained in connection with the operation of the Tavantolgoi deposit. However, this is not an advantage of ER but an opportunity enabled by obtaining the right to operate the Tavantolgoi deposit. Had the Government allowed ETT to have such an opportunity, ETT would have been able to raise financing on its own.

10.7 Regarding the Prepayment

Under Article 3.3 of the Investment Agreement, ER pays USD 200 million in prepayment to the Government and ETT with a 4.5 percent annual rate that will be offset from future tax payments and Cooperation payments. In other words, this prepayment is not an advanced payment but it is rather a loan with interests to be paid back.

For a certain period of time (3-4 years depending on mining and sales amount) until this prepayment is fully off-set, ER will not pay any taxes to Mongolia and cooperation payment to ETT.)

10.8 Financial Analysis of Mongolian Mining Corporation ("MMC")

MMC is domiciled in the Cayman Islands and is the parent company of Energy Resources LLC. Mr. Enkhsaikhan has provided the following response to the Members of Parliament regarding this matter.

On item 3.1 of the Appendix to the Government Letter No.3/81 issued on February 24, 2015, Mr. Enkhsaikhan has indicated that, "…Energy Resources LLC runs its operations in Tsogttsetsii soum of Umnogobi province and shares of its parent company Mongolia Mining Corporation is traded on the Hong Kong Stock Exchange with ticker 975, where 60% of the company's shares are owned by Mongolian citizens and entities". In addition, item 4.5 of the Appendix indicates that **"Mongolia Mining Corporation will participate in the Project through its subsidiary Energy Resources LLC**".

Thus, based on reports published by independent sources, we have reviewed the financial situation of MMC, which is participating in the TT bid through its subsidiary.

The following analysis has been based on reports published by independent rating agencies Standard & Poor's ("S&P") and Moody's regarding Mongolia Mining Corporation, a public company whose stocks are traded in Hong Stock Exchange with code 975, and past 3 year's financial statements of the company audited by KPMG.

10.8.1 "Standard & Poor's": Ratings Direct October 31 2014[8]

- Standard & Poor's outlook revision reflects the possibility of a positive or negative rating action over the next 12 months, depending on the completion of a proposed US$200 million in equity issuance. US$162 million of the proceeds would be sufficient for debt service. The rest of the proceeds, along with our estimate of cash balance of about US$60 million-US$70 million as of Sept. 30, 2014, and inventories, will likely be sufficient to absorb our current base case expectations of negative free operating cash flows over the next 12 months
- Although MMC intends to use the proceeds primarily for liquidity purpose, we also understand the company could use part of the funds to participate in a tender of a coal concession by the Mongolian Government. Downward rating pressure could persist, if the company uses a substantial portion of the proceeds on a tender or for other corporate purposes, leaving its debt repayment capacity to rely on still-thin operating cash flows.

[8] www.standardandpoors.com/ratingsdirect

- A further deterioration in MMC's operating cash flows because of a further slide in coal prices or a higher spending on deferred stripping could also erode the liquidity buffer despite the equity issuance.
  - We affirmed our 'CCC+' rating on MMC because we still consider the company's capital structure to be unsustainable. We project the company's debt-to-EBITDA ratio to remain well above 5.0x through 2015 even if MMC applies all proceeds from the equity issuance to debt repayment. We believe it would take further material positive developments for MMC's capital structure to become sustainable.
  - Debt-to-EBITDA ratio of 4.0 and above is considered high risk in international practice.
  - We believe it would take further material positive developments for MMC's capital structure to become sustainable, including a significant improvement in the operating outlook for coking or a further decline in costs, capital spending, or deferred stripping expenses. At this stage, we believe there is a limited likelihood of any of that materializing, given persisting oversupplied coking coal markets and a still weak pricing outlook. Significant cost reductions have also already taken place.

We believe MMC's obligations are currently vulnerable to nonpayment.

Liquidity

- We still assess MMC's liquidity as "weak"
- Our base case also remains that the company will be able to postpone the payments on US$105 million in promissory notes due to the Kerry Group. This is because Kerry Group has rolled over the payment multiple times over the past 12 months and we believe it remains committed to MMC's operations (shown in page 78 item 20 (iv) of MMC's 2015 Interim Report. We estimate about US$162 million of financial debt, excluding promissory notes, within the next 12 months.
- Negative free operating cash flows of US$70-80 million, including about US$50 million of capital spending and deferred stripping costs.

10.8.1 Moody's Research March 25 2015[9]

Moody's Investors Service stated that flat coking coal prices, continued debt servicing and higher operating costs weakened Mongolian Mining Corporation's (MMC, Caa2 negative) credit profile in 2014, and will continue to exert pressure in 2015.

Both MMC's revenue and sales volumes declined in 2014, as the average selling price of hard coking fell and the company lowered production. MMC's costs have risen for the following reasons:

[9] www.moodys.com/research

1. Increased transportation cost
2. Increased idling cost
3. Rise in fixed unit cost due to fall in production volume

In 2014, MMC's revenue declined by 25% to US$328 million, as the average selling price of hard coking coal fell 9%, in line with the industry trend.

MMC recorded an adjusted EBITDA loss of US$46 million in 2014, as its EBIT margin dropped sharply to -29% from 6% in 2013.

Further, although MMC's cash balance rose to US$253 million in 2014 from $77 million in 2013, Moody's expects the company will deplete its cash balance in the next 12 months.

1. In addition to expected negative operating cash flow of US$35-45 million
2. Maintenance capex of US$5-10 million
3. The company faces considerable debt servicing requirements, including US$115 million of short-term debt, and
4. US$70-80 million of interest expense.

MMC has a payable of US$190-205 million due in 2015.

In addition to falling revenue, MMC could deplete cash-on-hand by end of 2015 due to a higher rate of cash burn.

Stock and bond prices traded on the stock exchanges are indicative of the financial situation of the underlying company. Decline in MMC's stock prices since 2011 is due to the fall in coking coal prices in the international markets. It is also possible that the company's financial management had certain influence on MMC's stock performance.

Graph 1. MMC's stock performance since 2011[10]

[10] www.google.com

MMC's debt is US$1.02 billion as of year-end 2014, of which:

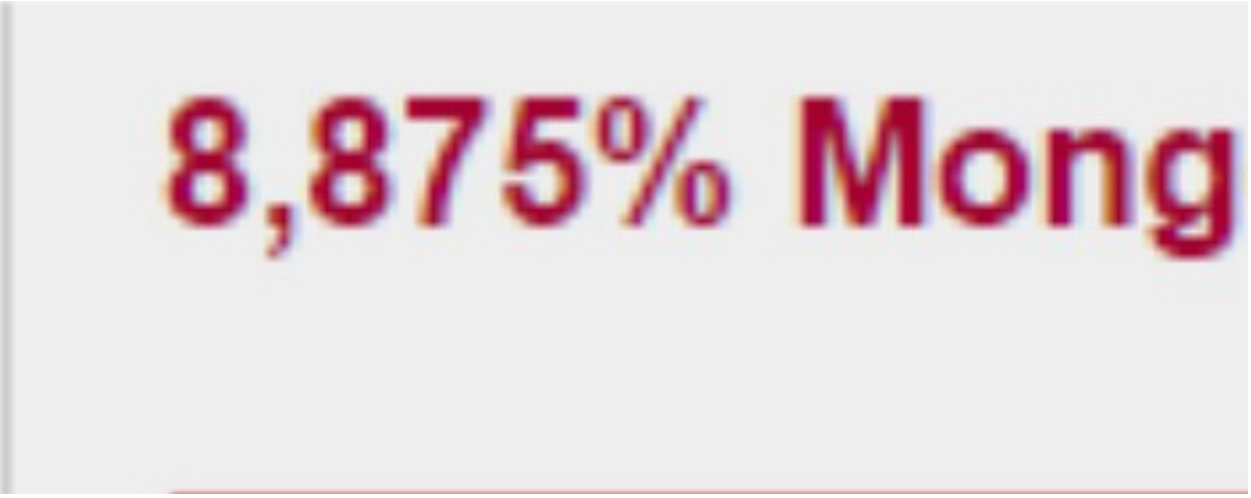
- US$320 million in short term debt
  - US$40 million in debt from Trade and Development Bank of Mongolia and others
  - US$298 million in promissory notes
- US$700 million in long term debt, of which:
  - Corporate bond issued on the Singapore Stock Exchange in the amount of US$ 600 million with yield of 8.875% payable in 2017
  - Loan from EBRD, BNP Paribas in the amount of US$103 million

Stocks of MMC's subsidiaries Mongolian Coal Corporation Limited (HK), Mongolian Coal Corporation S.a.r.l (Luxembourg) have been pledged as collateral for the bond. In addition, MMC's subsidiaries in Mongolia, Energy Resources Corporation LLC, Energy Resources LLC, Energy Resources Mining LLC and Transgobi LLC have provided financial guarantees on the bond.

MMC's bond has traded at US$55-79 with yield of 20-32% in the past year. If MMC were to raise capital now, its yield would be above 20% which is significantly higher than the yield of 8.875% on the bond issued in 2012, indicative of the company's financial difficulty.

As illustrated in Graph 2, although MMC's bond has been performing poorly since 2013, any news on the TT bid has impacted MMC's bond price positively.

Graph 2. Performance of MMC's corporate bond shown by 3 years and 1 year[11]



In 2014 MMC's equities amounted to US$396.8 while in 2013 equities were US$560.9 million.

Debt to equity ratio was 223.3% in end of 2014, whereas 159.9% in 2013.

Over-leveraged companies are considered to be at risk of insolvency and, further, bankruptcy as per international financial practice. As such global rating agencies, S&P and Moody's, has assigned low rating to MMC as they see the company's financial situation as unstable in the long term.

Acquiring the right to operate the Tavan Tolgoi mines would allow MMC to eliminate its competition and increase its coal reserves which would help its stock prices to recover and help the company overcome the current financial difficulty.

10.9 Baruun Naran Mine Acquisition by Mongolian Mining Corporation[12] (Translated from MMC annual report)

The Board wishes to announce that on May 31, 2011, the Buyer, a wholly-owned subsidiary of the Company, and the Company entered into a conditional Share Purchase Agreement with the Seller and Seller's Parent pursuant to which the Buyer has agreed to acquire the Sale Shares from the Seller for a total consideration of US$464,465,000, consisting of US$379,465,000 in cash payable by the Buyer to the Seller and US$85,000,000 by the issue of the Convertible Bond to be issued by the

[11] www.boerse-berlin.com

[12] Mongolian Mining Corporation, total outstanding shares purchase of QGX Coal Ltd, http://www.mmc.mn/upload/2012-11-27_e_00975ann-20121128.pdf

Company to QGX Holdings, subject to the Reserve Adjustment and the Royalty Provision pursuant to the terms of the Share Purchase Agreement.

The major terms of the Acquisition are set out below.

The share purchase agreement

Date:

May 31, 2011 (after trading hours)

Parties:

a) Mongolian Coal Corporation Limited as the buyer;
b) Quincunx (BVI) Ltd. as the seller;
c) Kerry Mining (Mongolia) as the seller's parent and guarantor for the Seller; and
d) the Company as the buyer's parent and guarantor for the Buyer.

The Seller is owned, indirectly, as to 90% by Kerry Mining (Mongolia) and 10% by MCS Minerals LLC. MCS Minerals LLC is owned as to 51% by Mr. Odjargal Jambaljamts (an executive Director and chairman of the Board) and as to 49% by MCS Holding LLC (the controlling shareholder of the Company). Save as disclosed, to the best of the knowledge, information and belief of the Board, and having made all reasonable enquires, the Seller and its ultimate beneficial owners are independent third parties who are independent of and not connected with the Directors, chief executive or substantial shareholders of the Company, its subsidiaries or any of their respective associates.

Subject matters:

The Sale Shares represent the entire issued share capital of the Target Company. Since the Target Company has yet to commence sales, no profit has been recorded. As at December 31, 2010 (being the date up to which the latest published audited accounts of the Target Company were made), the net asset value of the Sale Shares was approximately US$29,664,827.

Consideration:

The Consideration of US$464,465,000 is to be satisfied in the following manner:

(1) as to US$379,465,000[13] in cash payable by the Buyer to the Seller; and

(2) as to US$85,000,000 by the issue of the Convertible Bond by the Company to QGX Holdings.

Basis of the Consideration:

[13] A portion of the cash payable by the Buyer to the Seller is in the form of a promissory note with a 2-month maturity, Mongolian Mining Corporation, Discloseable Transaction in Relation to the Acquisition of the Entire Issued Share Capital in QGX Coal Ltd, page 3

The Consideration is determined after arm's length negotiations between the Buyer and the Seller after taking into account the Company's estimation of the total reserve, coal quality and mine development status in the Baruun Naran Coking Coal Mine, and potential commercial benefits of the Acquisition to the Company. The Directors are of the view that the Consideration is fair and reasonable and in the interests of the Company and the Shareholders as a whole. We expect to satisfy the Consideration via internal cash resources of the Group as well as the net proceeds of the initial public offering.

Completion:

Completion of the Acquisition will take place on or about June 1, 2011.

Information about Baruun Naran

The Target Company is a company incorporated in Gibraltar with limited liability on March 25, 2008, which ultimately owns the Baruun Naran Coking Coal Mine. The Baruun Naran Coking Coal Mine is located in southern Mongolia, Umnugobi Aimag (Southgobi province) approximately 500 km south of Ulaanbaatar, the capital of Mongolia, and around 60 km east of Dalanzadgad, the provincial center. It is located approximately 30 km from the UHG deposit.

According to the pre-feasibility study completed by Minarco MineConsult dated March 20, 2008, the indicated and measured resources of the Baruun Naran Coking Coal Mine, measured in accordance with National Instrument 43-101, the (Canadian) Standards of Disclosures for Mineral Projects, were estimated at approximately 253 mt of measured and indicated coal resources and 193 mt of potential mineable coal.

Commissioning of the Baruun Naran coking coal mine[14]

The board of directors (the "Board") of Mongolian Mining Corporation (the "Company") is pleased to announce that the Baruun Naran ("BN") Coking Coal Mine (the "BN mine") of the Company has been successfully commissioned by the State Commission comprised of specialists from various government agencies of Mongolia on February 1, 2012. Khangad Exploration LLC, an indirect wholly-owned subsidiary of the Company is the registered holder of the Mining License No.14493A which gives the Company exclusive right to conduct mining activities throughout the license area of approximately 4,482 hectares at the BN mine for an initial period of thirty years from December 1, 2008.

The Company targets to mine 1.0 million tonnes run-of-mine ("ROM") coal by December 31, 2012 from the BN coking coal deposit. The Company plans to transport ROM coal from the BN mine to the UHG mine for processing at its Coal Handling and Preparation Plant ("CHPP") located at the UHG mine for further marketing as washed coking coal product to its customers in the People's Republic of China.

[14] Mongolian Mining Corporation, Commissioning of the Baruun Naran Coking Coal Mine, http://www.mmc.mn/upload/2012-02-02_e_00975ann-20120202.pdf

Impairment loss[15]

On March 22, 2015, the board of directors (the "Board") informed the shareholders and potential investors of the Company that based on the preliminary discussion with the auditors of the Company, it is expected that the Company will make a provision for impairment losses on non-financial assets for the financial year ended December 31, 2014 (the "Impairment").

Based on careful consideration of the Board and the Audit Committee and communication with the auditors, the Impairment will be approximately US$190 million, recognized in relation to the acquired mining rights [Baruun Naran] under the intangible assets based on the preliminary assessment of the Board and its discussions with the auditors of the Company regarding the consolidated accounts of the Group for the financial year ended December 31, 2014 and other information currently available.

According to the Company 2014 Annual Report and in accordance with IAS 36 Impairment of Assets, entity shall assess at the end of each reporting period whether its assets are carried at value no more than their recoverable amount. Thus, the Company has undertaken a review on the carrying amount of the Group's property, plant and equipment, construction in progress and intangible assets, with reference to independent valuation report; and impairment loss of US$190 million was recognized in relation to the BN mining right, considering the prolonged weakening global coking coal prices due to the supply and demand imbalances. The Impairment is an accounting related adjustment and a non-cash item and therefore, will not have any impact on the cash flow of the Company[16]

Based on the summary, impairment loss of US$190 million of the Baruun Naran mine was recognized where MMC has purchased the mine for US$464,465,000. MMC is at loss for amount equivalent to difference in value. "Kerry Mining" has made profit of US$204,465,000[17] by purchasing the mine for US$260 million and selling it for US$464,465,000. Therefore, Working Group considers that Baruun Naran mine acquisition needs to be clarified in detail.

Eleven. Construction and investment in the infrastructure of the Tavantolgoi deposit and determination of an economically viable method for Mongolia

"BNP Paribas" acted as the financial advisor for the Mongolian New Railroad Project, and it issued a financial model in 2014. Under the financial model, railway transportation tariffs for 1 ton/km will be 3.8 cents and project IRR (Internal rate of

[15] Mongolian Mining Corporation, Impairment Loss, http://www.mmc.mn/upload/2015-03-22_e_00975ann-20150322.pdf

[16] Mongolian Mining Corporation 2014 Annual Report, page 45, 113, 147, http://www.mmc.mn/upload/2015-04-21_EW101.pdf

[17] http://www.reuters.com/article/2011/05/31/qgx-mmc-idUSL3E7GV2WF20110531

return) will be 14%, so the investment is recoverable within 12 years. Australia's "AECOM" made a feasibility study in 2013 and this feasibility study calculated that IRR (Internal rate of return) would be 10% for the intended railway when total transportation for one year is 30 million tons and transportation tarffis for 1 ton/km is 3.3 cents.

If the railway base structure that has special importance to the society and economy of the country stays in ownership of state owned legal entity and is used by it, railway will accumulate income in the state budget from the year of its first use and will build up economically profitable and advantageous condition. For example, it was calculated that the railway in the direction of the Ukhaa Khudag-Gashuun Sukhait will produce 1.9 billion USD of dividend in addition to the taxes paid, within 25 years.

Another benefit of state ownership is to accumulate investment for other railways routes as provided in the "State Railway Policy" stage by stage.

As stated in Article 6.2 of the Railway Transportation Law and Government Resolution number 121 dated 3 November 2012, the railway base structure in the direction of Ukhaa Khudag – Gashuun Sukhait was determined as the base structure of special importance to the society and economy of the country.

This railway base structure will accumulate income in the state budget from the year of its first use.

The Ukhaa Khudag-Gashuun Sukhait railway, in itself, has the potential to accumulate USD 1.9 billion through dividends in addition to the taxes paid, within 25 years and to raise investment for other railways in different directions as stated in the "State Railway Policy".

Main indicators are shown in below table (Source of information: source is provided by "MTZ" JSC):

Indicators	**State ownership predominant company with special purpose**	**As stated in the Government Resolution 268**
Concession period	25-30 years	30 years
Portion to be transferred to state	100%	51%
Participation of state and private sector during the concession term	State ownership 51%	100% in the ownership of subsidiary of foreign invested company with joint participation of private sector
Dividend distributable to state	USD 1.9 billion within 25 years according to portion of participation	None
Economic profit (IRR)	13%	Unclear
Transportation rate	Same rate for all transporters	As stated in Article 11.3 of the Railway Concession Agreement, owner of the railway base structure has a right to set

		transportation rate solely and independently according to market principles, in compliance with legislations.
Project investment	Valuation of railway protected strip land, valuation of concession right, valuation of the right of signature approved agreement, owner's equity, investment loan	(As stated in Article 5.2(b) of the Railway Concession Agreement, raise investment by creating security in railway base construction, license, and rolling stock)
Burden on the state budget	In case valuation of trackside and concession right is made no additional asset will be required. The state budged will not be loaded.	The state budged will not be burdened but will not be profitable.
Benefit and market competition	Initial state ownership will build economic ground for development of railways in other directions.	Closed market competition

With Government Resolution number 121 dated 3 November 2012, the Government decided that the railway base structure to be constructed during the first stage as stated in Article 3.2.2 of the State Railway Policy and the railway base structure to be constructed during the second stage as stated in Article 3.2.4 of the State Railway Policy are to be designated as railway base structures with special importance to the society and economy of the country; and such railway base structures shall be constructed under a united management and coordination by way of incorporating a company with special purpose consisting of domestic and foreign investors.

Moreover, the National Security Council's Recommendation number 35/32 of 2011 and Recommendation number 07/04 of 2013 provide that abovementioned railway base structures must be built through a concession that is directly granted to a state owned or predominantly state owned company and must be kept under state ownership in accordance with the State Railway Policy.

The "Mongoliin tumur zam" state owned JSC, which is implementing the New Railway Project and structure of this project has been in full compliance with the provisions of the resolutions above. Under the Annex of the Government Resolution number 121 of 2012, it is planned that 40% of the project assets should be owner's equity and 60% of it should be financed through loans, and by allowing 51% of the owner's equity to be financed by the Government the railway base structure can be under the control of a state ownership predominated legal entity in accordance with related legislations.

The total investment of the railway base structure in the direction of Ukhaa Khudag – Gashuun Sukhait is USD 1 billion, and the Government of Mongolia has invested USD 212 million, which is equal to 51% of the planned owner's equity.

As provided in the Government Resolution No. 121 of 2012, the remaining 49% of owner's equity investment of the railway base structure in the direction of Ukhaa Khudag – Gashuun Sukhait is open to domestic and foreign investors, and rest of the investment may be jointly financed.

There is a big risk of limiting market competition if the miner, transporter, and buyer of coal are the same entity.

When cooperating with domestic and foreign investors on railway field issues, it will be appropriate if Mongolian side negotiates for deal structures that are beneficial to Mongolia such as the inclusion of valuation of railway protected strip land, valuation of concession right, raising equity capital by selling the 49 percent and signing bonus, and etc.

On 21 May 2015 Parliament made amendments to the Fiscal Stability Law. Under this amendment, any loans or debt guarantee agreements under which the Government invests in an energy, mining, or railway entity by borrowing funds from those entities which will be repaid from the proceeds shall not be included in the Government Debt Limit. Therefore, the Government has the ability to issue guarantees for the financing of railway projects and raise funds. It is imperative that the Government uses this advantage.

Twelve. Determining the most beneficial conditions in implementing the Railway Transit Transportation Agreement signed with the PRC,

Article 1.5 of the Parliament Resolution number 39 of July 7, 2010 on "Matters regarding the usage of Tavantolgoi Coal Deposit" states that transit transportation and conditions precedents must be negotiated. In accordance with this provision the Government is supposed to negotiate with the investor the terms and conditions of the transit transportation.

However, 7.1(k) of the Investment Agreement provides that the Government will be responsible for the facilitation of transit transportation of the coal from Mongolia by providing quick customs clearance and access to maritime ports in accordance with Mongolian and international laws. This provision puts the responsibility that must have been negotiated with the Investor only on the Government.

If the Investor has no responsibility with regards to the transit transportation then it is advisable that the Government uses this possibility and shifts this responsibility to MTZ JSC to monetize from the transportation activities.

During the state-visit of Xi Jingping, the ministries for transportation of Mongolia and China signed a cooperation agreement in the rail transit sector on August 22, 2014.

Article 3 of the agreement provides that China will offer large discounts beneficial to Mongolia on transit tariffs for commodities and products shipped through China. This agreement has opened up the possibility for Mongolian mineral products to be competitive on third country markets.

Since the adoption of the rail gauge standard by Parliament on October 2014, there has been a rise in interest from Chinese and Japanese large scale companies and consortiums; therefore, there is possibility to attract investment for the railway project separately from the Tavantolgoi deposit and without burdening the state budget.

Government Resolution No.268 granted the concession holder of the Tavantolgoi-Gashuun Sukhait railway to own and operate the railway for 30 years from the date of its commission. The concession holder was then to transfer 51% of the stake to the state after 30 years. The conditions set out in Resolution No. 268 do not align with the national security interests of Mongolia. In addition, allowing for the possibility that only one entity will extract, transport, and purchase coal may pose a risk that hinders the transportation of other entities' commodities and products.

Granting a private entity the concession for such a long time to **build-own-operate-transfer** this railway infrastructure that has an extraordinary importance to Mongolia's exports and socio-economic conditions may limit the implementation of the State Railway Policy in accordance with national security interests and Mongolia's genuine national interests.

Furthermore, provisions 11.2(b) and (c) of the Investment Agreement provides that transportation activities may be done **foreign subcontractors and through foreign labor**. It is the opinion that these provisions were meant to hand over the railway transportation to foreign companies.

It is no secret that the railway will connect to Shenhua's railway from the Chinese side, and that Shenhua will conduct the transportation activity. This was made clear by Minister M.Enkhsaikhan's letter dated January 26, 2015 responding to the Democratic Party's caucus.

In the letter, Minister M.Enkhsaikhan stated, "China Shenhua Energy will be the main logistics provider for the sale of Tavantolgoi's commodities in China by using its existing railway infrastructure, sales organization, and access to maritime ports in place".

Under this scenario there will be no income for Mongolia from the railway transit.

Mongolian Railway ("MTZ") state owned JSC, has been implementing the new railway project in accordance with the aforementioned legislations and regulations.

Government Resolution No. 121 of 2012 provided that the Project shall be financed by 40% from own capital and 60% from loans and debts. The Resolution also resolved that 51% of the own capital will be financed by the Government of Mongolia. In

accordance with the relevant laws and resolutions the infrastructure was to be majority owned by a state owned entity.

Therefore, the Working Group has decided that in accordance with Government Resolution No.121 of 2012 that the new railway infrastructure's 51% should be owned by MTZ and the remaining 49% should be owned, left open for investment, or for cooperation for domestic and foreign entities.

This will fulfill the requirements of Parliament Resolution 32 dated June 24, 2010 on the construction of new railway; Resolution 48 dated 2010 on the Concept of Mongolia's National Security; National Security Council's Guidelines No. 35/32 of 2011; and Government Resolutions No. 121 dated November 3, 2012 and No. 28 dated January 26, 2013.

Thirteen. Request information from international and domestic banks, financial institutions, stock exchanges, relevant companies, organizations, and individuals in order to conclude an opinion.

The Working Group has requested and received information from the Government Cabinet, Ministry of Foreign Affairs, Ministry of Mining, Ministry of Environment, Green Development, and Tourism, Ministry of Roads and Transportation, the Financial Regulatory Commission, MTZ, and Erdenes Tavantolgoi. In addition, the official positions of Open Society Forum NGO, Mongol 999 consortium were taken into consideration. (*The official responses are attached*).

The Working Group has on numerous occasion requested the following agreements from the Government and relevant companies but were not provided: ER and China Shenhua Energy's agreement to jointly establish a company, agreement to establish a trading company with Japan's Sumimoto, transfer of rights agreement between Erdenes Tavantolgoi and ER.

Fourteen. To provide other relevant opinions and conclusions

14.1 Regarding Government Resolution No. 268 of 2014 on taking actions regarding the Tavantolgoi deposit.

Government Resolution No. 268 of 2014 is violating the following Parliamentary resolutions, National Security Concept of Mongolia, and Government Resolutions:

14.1.1. Government Resolution No. 268 Article 1(e) states, "First, to construct the Tavantolgoi-Gashuunsukhait railway, and to transfer 51%, free of charge, after 30 years since commissioning to the state on a build-own-operate-transfer concession agreement in accordance with the Concession Law of Mongolia. After the commissioning of the Tavantolgoi-Gashuunsukhait railway, in consideration of the coking coal market conditions allow the investor to partake in the Tavantolgoi-Sainshand railway project."

This provision conflicts with the following:

- Article 6.2 of the Railway Transit Law, "**Railway infrastructures that are of great importance to the nation's economy and society must be owned by the state or majority state owned companies or must be transferred to the state or majority state owned company upon a certain period.**"

- 2.2 of the Parliament Resolution No. 32 of 2010 on the State Policy on Railways, "**Railway infrastructures that are of great importance to the nation's economy and society must be under state ownership in accordance with Article 6.2 of the Railway Transit Law**."

- Provision 1 of the National Security Concept Recommendation of Mongolia 35/32 of 2011, "**as provided under Parliament Resolution No. 32 of 2010 on the State Railway Policy, the concession for the railway infrastructure must be awarded to a state owned or majority state owned entity in accordance with 17.1.1 of the Concession Law.**"

- Section 2.1 of the National Security Concept Recommendation 07/04 of 2012, "In order to implement National Security Concept 38/32 of 2011, the concession shall be awarded on a direct contracts basis." (*Copy of the Recommendation is attached*)

- Based on Article 6.2 of the Railway Transit Law and the National Security Concepts, the Government issued Resolution No. 121 of 2012 that authorized MTZ, 100% state owned entity, to build phase 1 and 2 of the Ukhaa Khudag-Gashuunsukhait railway, since such infrastructure is of great importance to the nation's economy and society.

- Government Resolution No.28 of 2013 that authorized MTZ to build phase 1 and 2 of the railway infrastructure as approved by State Policy on Railways on a build-operate-transfer basis.

Thus, the Government has no legal basis to transfer the right to build the Ukhaa Khudag- Gashuunsukhait railway from MTZ to a different legal entity.

14.1.2 Government Resolution No. 268 Article 1(j) states, "Within the framework of the investment agreement, the investor's 51% must have at least for the last five years extracted, produced, transported, and exported within the territory of Mongolia, and at least a controlling stake of the investor must have been owned for the last five years by Mongolian individuals.

This provision conflicts with the following:

- Provision 1.1 of the Parliament Resolution No. 39 of 2010, "The extraction of the Tavantolgoi deposit must be done by **a state owned entity**, to establish Erdenes Tavantogloi as a subsidiary and transfer its mining license without dividing and to enter into an investment agreement with it, and to contract an **operator do extraction works for a certain period**."

- Parliament Resolution No. 37 of 2012 on Government Action Plan for 2012-2016, "To leave Tavantolgoi under state control, to enter into an **extraction operating agreement** with domestic or international counterparts."

An extraction operation is the act of extracting coal from the ground, and not such a large scale activity mentioned above. Therefore, provision 1.1 of the Parliament Resolution No. 39 of 2010 specifically provided that the extraction operations may be done for a certain period.

14.1.3 Article 3.4(a) of the Investment Agreement provides that the **Chalco agreement will not be assigned to ER but that Chalco and ETT will remain parties to the Chalco agreement**.

This Article directly violates provision 1(g) of the Government Resolution No. 268 of 2014, which provides, "The investor shall assume and perform the remaining obligations and loans of Erdenes Tavantolgoi to China's Chalco under Chalco agreement". In other words, the terms and conditions stipulated under the Government Resolution No. 268 decision to initiate open competitive bidding for investors and co-operations on the Tavantolgoi deposit has been directly violated.

Government Resolution No. 268 of 2014 on taking actions regarding the Tavantolgoi Deposit is violating the Parliament Resolution 40 of 2008, Article 2.2 of the Parliament Resolution No. 32 of 2012, Parliament Resolution No. 37 of 2012 on the Government Action Plan for 2012-2016's provision stating that Tavantolgoi deposit must be mined in cooperation with domestic and foreign investors, the National Security Concept of Mongolia 35/32 of 2011, 07/04 of 2012, and 04/03 of 2015, Government Resolution No. 121 of 2012, and Government Resolution No.28 of 2013 granting concession to MTZ. Thus, Working Group is of the opinion that because of these violations, Resolution No. 268 should be invalidated in accordance with Article 45.2 of the Constitution of Mongolia. *(the aforementioned resolutions are attached)*

If Government Resolution No. 268 is not invalidated, the Government and ETT would be liable for knowingly and falsely representing to the Investors that the Investment Agreement is in compliance with the above mentioned governmental resolutions.

Because ETT under 10.1(b) Cooperation Agreement and the Government under 21.1(e) of the Investment Agreement have represented and warranted that all necessary actions has been taken to fulfill their contractual requirements, agreements

were executed in accordance with Mongolian laws, and that no laws have been violated.

14.2 Regarding the structure of the investor

The drafts of the Cooperation Agreement and the Investment Agreement for the mining of the Tavantolgoi deposit is to be concluded between Mongolia's state owned entity Erdenes Tavantolgoi ("ETT") and Luxemburg's Mongolian Coal Corporation's 100% owned subsidiary Energy Resource Corporation, Energy Resource Corporation's 100% owned subsidiary Energy Resources LLC and China's state owned China Shenhua Energy Company Limited ("Shenhua").

On section 2 of the Cooperation Agreement and on section 5 of the Investment Agreement, Energy Resources LLC was defined as the Project Company. In other words, Energy Resources LLC (ER), Energy Resources Corporation (ERC), and Shenhua are supposedly the consortium that is making up the Project Company, but in fact, the Project Company is the current miner of Ukhaa Khudag deposit, Energy Resources LLC.

The Project Company's 51% will be owned by Energy Resources Corporation and 49% will be owned by Shenhua. Investment Agreement summary of events section (H).

Energy Resources LLC is 100% owned by Energy Resources Corporation, whereas, Energy Resources Corporation is 100% owned by Luxemburg's Mongolian Coal Corporation, Luxemburg's Mongolian Coal Corporation is 100% owned by Hong Kong's Mongolian Coal Corporation Limited, Mongolian Mining Corporation Limited is a subsidiary of the Cayman's Mongolian Mining Corporation.

As stipulated in the agreement ER is made up of its investor Energy Resource Corporation and Shenhua. In other words, these companies will be the investors that will mine the Tavantolgoi deposit.

Energy Resources Corporation will be 100% owned by a foreign investor and is foreign invested entity because in accordance with 3.1.5 of the Investment Law, "a foreign invested entity is an entity that owns 25% or more of the outstanding shares of a company incorporated under Mongolian law, and each foreign investor's contributed capital should be at least US$100,000."

Since Energy Resources Corporation is under 100% control of foreign investors and Shenhua is a foreign entity, the Project Company ER is directly and indirectly under the 100% control of foreign legal entities.

14.3 Regarding the Investors assets and shares being pledged

As mentioned in this Opinion at 10.6, ER's investment in Ukhaa Khudag was calculated towards the investment amount of USD 1 billion.

Minister M.Enkhsaikhan was talking about mining equipment, coal washing plant, water facilities, and power plants as basic investments, but these assets are already in use at Ukhaa Khudag mined by ER.

However, these assets that were calculated towards the investment such as mining equipment, coal washing plant, water facilities, power plant, cash, and products are all pledged as security under a USD 570 million loan from EBRD, FMO (Netherlands), DEG (Germany), BNP Paribas, BNP and ICBC. *(Source: upload.mmc.mn/financial report) KPMG audit report.*

In addition, the shares of Mongolian Coal Corporation (Hong Kong) and Mongolian Coal Corporation (Luxemburg), the owners of ERC, have been pledged as security for their parent company Cayman's Mongolian Mining Corporation's bond issuance. *(Source: upload.mmc.mn/financial report) KPMG audit report.*

Since ERC's, the 51% stakeholder in the Project Company, shares have been pleged by MMC, its parent company, as collateral to their loan, the Working Group deems Project Company as financially not fit.

14.4 Luxemburg's 100% invested Energy Resource Corporation did not participate in the bidding process for the Tavantolgoi deposit.

Article 1.5(d) of the Parliament Resolution No. 39 of 2010 stated that negotiations for the conditions of the transit transportation, conditions precedents, upfront payments, port usage, investment, and sales should be done, and that a consortium of domestic and foreign investors should be selected through an open bidding process. The resolution further provided that the investment agreement and other documents should be introduced for debate at the 2010 Parliamentary Fall Session.

Even Government Resolution 268 of 2014 referenced Parliament Resolution 39 under Article 1. It stated to continue the open bidding process for the Tavantolgoi deposit in accordance with Parliament Resolution 39 of 2010's conditions and requirements used for the open bidding process on December 8, 2010.

Looking at the Government Resolution, it is continuing the open bidding process announced in 2010. Under the 2010 bidding process, 6 candidates were short listed; 1) consortium of Shenhua (China) and Mitsui (Japan), 2) Peabody Enery, 3) Russian Railway Company, SUEK (Russia), Japanese consortium, Korean consortium, 4) Vale (Brazil), 5) Xtrata Coal (Australia), 6) Arcelormittal (Luxemburg).

The second stage of the bidding process continued between these 6 candidates. However, ERC who had not even proposed a bid in the first round is not 51% stakeholder in the Project Company in the project agreement.

ERC is not included in the agreement to enter into the bidding process for Tavantolgoi deposit between Energy Resources LLC, Shenhua, and Sumimoto signed on December 1, 2014. However, in the Investment Agreement and other relevant agreements ERC is a signatory.

Minister M.Enkhsaihan explained in the Parliamentary hearing before 16 MPs that MMC will participate in the Project through its subsidiary Energy Resources LLC.

Minister M.Enkhsaihan's explanations have been proven right by Mr. J.Odjargal, the chairman of the board of directors of MMC. In his letter to the shareholders dated March 15, 2015, Mr. Odjargal stated that it was a pleasure to organize and lead the consortium comprised of Shenhua Energy Development Limited and Sumimoto Corporation. (*Source: MMC 2014 Annual Report*)

Cayman's MMC, its subsidiary Luxemburg's ERC, and ERC's subsidiary ER did not participate in the 2010 competitive open bidding process for the Tavantogloi deposit.

14.5 Regarding Conflicts of Interests

ER and ETT both possess licenses to mine the Tavantolgoi deposit. They both mine the same coal and deliver it to the same market. They are competitors and have direct conflict of interests.

In this regard, in preparing the requirements for the consortiums bidding for the Tavantolgoi deposit, the Government under Article 1.2 of its Government Resolution No. 59 of 2010 specifically provided that legal entities with a conflict of interest should not be allowed to bid.

The Government, by awarding ER, a direct business competitor with a conflict of interest to ETT, the project to mine the Tavantogloi deposit has violated Government Resolution 59 of 2010.

14.6 Regarding the term of the Cooperation and Investment Agreements

Articles 4.1(a) and (b) of the Cooperation Agreement provide that the term of the Cooperation Agreement shall be in effect during the **term of the Investment Agreement**, and that the term Cooperation Agreement shall always be in line with the term of the Investment Agreement. The terms of these two agreements are closely related to each other. The Investment Agreement is for a term of 30 years with the option for another 30 years.

Article 4.1 (a) and (b) provide that the Investment Agreement shall be for a term of 30 years, with an option for extension of another 30 years. In addition, Article 4.1(h) disallows the shortening of the term. Meaning this agreement is guaranteed to last at least 30 years.

The provision that stated that the term of the Agreement **may be extended until the investments are recuperated** under Article 4.1 (e) of the Agreement of April 6, 2015 has been omitted in the April 23, 2015 version of the Agreement.

However, under Article 2.2(a) of the Investment Agreement, ER will conduct additional exploration to increase the reserves, and as provided under Article 4.1(f) **the**

parties will come to a mutual agreement on extending the term until ER recuperates its exploration investments. (*This provision is more flexible compared to the April 6, 2015 version of the Agreement that provided that ER will retain the right to extend the Agreement until it had recuperated its exploration investments.*)

More importantly, under Article 2.1(d) of the Investment Agreement, ER has **full discretion in planning the exploration and issue reports on it**. Exploration costs are very high, and ER may use this to its own advantage.

Looking at these provisions, ER may increase its investment by including the costs associated with exploration, and if such exploration costs are not recuperated within the initial 30 year and additional 30 years terms, ER will, until the time it has recuperated its cost, **indefinitely extend the term of the contract.**

But this provision is inconsistent with Article 2.2 (d) of the Agreement, which provides that **exploration costs will be deducted from taxable income as provided under Article 9.2(l)**.

Since, under 2.2(d) ER is deducting its explorations costs from taxable income, it will not incur any losses. Thus, there should be no issue about recuperating exploration costs between the parties.

14.7 Regarding pledge rights

Article 6.1(n) of the Investment Agreement allows **ER to pledge or transfer its rights and benefits under the Agreement to its lenders**. (*the terms interests and investors has been omitted in this version of the Investment Agreement compared to the one of April 23, 2015.*)

However, Article 8.1 (b) of the Cooperation Agreement states that ER and the Investors have the right to transfer their rights, interests, and benefits provided in the Cooperation Agreement to the **Investors or lenders** in order to raise funds.

In addition, **Article 8.3(b)** allows the Investors and ER to issue security interests over their rights, interests, extracted and processed products from Tsankhi, coal washing plant, power infrastructure, other buildings, construction sites, and other assets of the Project.

Articles 8.4(c)(i) and (ii), 8.4(d) (i), (iv), and (vi), 8.5(a), 14.1(a) were included to ensure the above mentioned provisions of the agreement.

These are the most serious articles of the Investment Agreement. **Especially, 8.4(c)(ii) and (d)(vi), which allow the Lenders to gain control over the Project, ER, and the Agreement or assign the Agreement to third parties, or transfer ER's rights and obligations to a third party in the event ER defaults on its obligations. 8.4(d) provides that upon the Lender's request the Government shall directly enter into a contract with the Lender.**

The Mongolian side has no oversight capacity over this because:

- The Agreement's introductory part D and Articles 1.1 (a) and (b), 1.2 (a), and 6.1(d) provide that ETT will transfer its **license to operate, all rights, entitlements, and duties with regards to mining activities, and its land possession rights to ER over the term of the Agreement**. (Cooperation and Investment Agreements provide for a term of 30 years, with option to extend for another 30 years).

- **ER will have the right to mine from the Tavantolgoi deposit, to amend the feasibility study, to determine the costs associated with development, construction and mining activities, and to identify the investment conditions**. (Cooperation Agreement 5.1(n)). **Furthermore, ER will have the exclusive right and control over exports, sale, transportation, and marketing of the extracted and processed coal.** (Cooperation Agreement 5.1(d)).

- ER retains the right **to prepare project development plan and construction plan** (Investment Agreement 4.2(a)) **and the right to identify the investment timeline and to amend or change it.** (Investment Agreement 4.3(a) and 4.3(c)).

- ER **has the sole right to make decisions on the sale of products such as to decide how much extraction it will make in a year and how much coal to process; to choose the markets for sale; to determine the costs and valuation of processed products; to determine the volume and prices of the products for sale; and to determine the rate and costs associated with transportation agreements.** (Investment Agreement 2.4(b) and 2.5(b)).

- ER will mine coal, process, dispose of, transport, export, sell coal, to market, find financing, make investments, create security interest, build railways, use railway transportation, conduct additional exploration, exploit proven resources, and build infrastructure for extraction. (Investment Agreement 2.1(b), 2.2(a) and (c)).

- Finally, the Investment Agreement leaves up to the discretion of ER to prepare the detailed mine plan, mine activity costs, and investment conditions. (Investment Agreement 2.1(c)). ER will determine, on its discretion, the scope of the mine activity, the calculations for the development of the mine, **exploration plans, and the relevant reports**.

Therefore, all of the above mentioned **rights and entitlements** given to ER for a term of 30 years might be pledged and transferred to 1) the Investors or 2) the lenders.

The Investors are defined as Energy Resources Corporation, 100% owned by Luxemburg's Mongolian Coal Corporation, and China's state owned Shenhua in the Investment Agreement.

Lenders are defined as entities that are lending to ER such as China and Japan's export banking agencies, development banks, commercial banks and other multi-faceted financial institutions including international investors, banks, and institutions under 30.1(g) of the Investment Agreement.

Articles 8.4(c)(ii) and (d)(vi) allow the Lenders to gain control over the Project, ER, and the Agreement or assign the Agreement to third parties, or transfer ER's rights and obligations to a third party in the event ER defaults on its obligations. These provisions show that ER is planning to make reality of this case. In accordance with these provisions ER was planning to exit the Investment Agreement and other agreements.

Article 8.4(c)(ii) provides that it is enough for ER to default, deliberately or without, on its obligations to the Lenders and Investors, to transfer all its rights, interests, and assets to the Lenders.

But Article 8.2(b) of the Cooperation Agreement and Article 5.3(a) of the Investment Agreement have barred the lawful owner of the Tavantolgoi deposit, ETT, from creating any security interests. In short, whereas, ER retains the full right to pledge its rights, interests, and assets, the state owned ETT does not enjoy the same right.

The Article 14.1 of Investment Agreement version of April 6, 2015 stated that the foreign investor may transfer its **Contractual rights to Shenhua Group Corporation Limited or dispose of it in any manner.** This was changed in the April 23, 2015 version under Article 6.1(n) by providing that the **Project Company (ER) may pledge or transfer its contractual rights and benefits to the Lenders.**

Article 14.1(a)(i) of the Investment Agreement provides that the Project Company may fully or partially transfer its contractual rights, duties, and license to an affiliated entity, or pledge or transfer to the Lenders as provided in Articles 6.1(n) or 8.5 of the Investment Agreement. In all over cases, the Project Company may not transfer its contractual rights to third parties without the consent of the Government.

The prior version and this version's only difference is **that Shenhua Group Corporation Limited** has been removed. Moreover, these provisions were inserted to ensure ER's right to pledge or transfer its contractual rights to the Lenders or affiliated entities without governmental approval.

Article 14.1 titled "Transfer of Rights and Duties" of the Investment Agreement is a preface to accomplish this. Thus, it is our opinion that the Government and ETT may not, in any event, agree to this provision.

14.8 Regarding the usage of water

Articles 2.7(b),(c) and 5.5(c) of the Investment Agreement provide that the Government has agreed and allowed ER to use Balgasiin Ulaan Lake for industrial purposes and to construct and own water systems and aquifers and to have the **right to first use of the water**. In the event, the Government is obliged to supply water, the Government must ensure **supply of up to standard water on an adequate and consistent basis**.

Balgasiin Ulaan Lake is located in Khankhongor soum of Umnu-Gobi province and is 45-60km south-east of Dalanzadgad. It is considered as one of the larger aquifers of the Gobi. The aquifer is 20km long and 5-8.61 km wide.

The Government may not be obliged to supply ER with running and constant water. Because the representatives of the province took the aquifer under special protection by passing Resolution No. 7/8 of 2010. (*Resolution is attached*).

In addition, the National Security Council issued Guideline 34/28 in 2010 on "The protection of water aquifers". Under section 2 of the Guideline it considered the aquifer underneath Balgasiin Ulaan Lake as a significant aquifer and recommended to take it under special protection through a Parliamentary Resolution by directing the Government.

Mr. L.Batchuluun, the head of the representatives' council of the Umnu-Gobi province, issued a letter to the Speaker of the Parliament, Mr. Z. Enkhbold, reasoning that the aquifer should still be under special protection due the shortage of drinking water in the province and the potential impact on the health and well-being of the 20 thousand inhabitants of the provincial capital.

The Working Group asked for more information on this from the Ministry of Environment, Green Development, and Tourism. The Ministry replied with letter 08/3026 dated May 26, 2015 and explained that until 2020 water usage of the proven resources of 404,19 l/s with a usage of 151 l/s wont damage the environment. It recommended that for the coal washing plant clean aquifers in Gobi region should not be used, but rather deep ground water with high minerals should be used.

In addition, citizens of the Khankhongor soum, located next to Balgasiin Ulaan Lake, in a public forum adopted Resolution 11 on October 5, 2013 disallowing the usage of the aquifer for mining purposes. (a *copy of the resolution is attached*)

On December 5, 2013 the representative's council of Khankhongor soum supported the resolution 11 of the public forum that disallowed the usage of the aquifer for mining purposes and issued their own Resolution No. 47. (a copy of the resolution is attached).

On May 12, 2015 the citizens of Khankhongor soum and decided in public forum to disallow the usage of Balgasiin Ulaan Lake's water for mining purposes and supported the use of a dry technology for processing/washing of the coal.

ETT has entered into a memorandum and is working with Japan's Nagata Engineering to introduce a dry technology for washing coal. Within this framework, samples from the 0 and 4th seams were sent to test whether it would get processed. Furthermore, a pre-feasibility study has been conducted to wash 5 million tons of coal a year, and the testing team is preparing to build a small scale plant at Tavantolgoi deposit.

Therefore, whichever entity is going to exploit the Tavantolgoi deposit must conduct further studies regarding the usage of aquifers.

14.9 Regarding the overlap of the licenses for Tsankhi and Borteeg

ETT possesses the following 8 mining licenses covering a total are of 68481.5 ha : MV-011943 (2,046.4 ha), MV-016883 (700.39 ha), MV-016881 (556.72 ha), MV-016882 (2447.13 ha), MV-011953 (12864.47 ha), MV-011954 (22901.37 ha), MV-011955(23813.1 ha), and MV-011956 (3151.92 ha).

Tavantolgoi deposit is made up of the following fields Tsankhi, Uhaakhudag, Borteeg, Onchkharaat, Oortsog, and Bortolgoi. **Out of these, Tsankhi is the only one that has been explored in detail and is ready for extraction.**

Section B of the Cooperation Agreement and Section B of the Investment Agreement both mentioned the license of ETT's possession.

4 minerals licenses named MV-011943, MV-016881, MV-016882, and MV-016882 covering an area of 5740.57 hectares in Umnu-Gobi province are designated as Tsankhi's mining licenses.

Even though the Agreement states that these 4 licenses are designated as Tsankhi, in fact, some parts overlap with Borteeg's area. The overlapped area covers 1786.98 ha, and consists of 526.6 million tons under A+B+C levels and 203 million tons under A+B+C+P1 levels for a total of 728.7 million tons of coking and thermal coal. It is inherent that these resources will only grow upon further exploration. (Based on ETT information provided to on June 12, 2015 #01/788).

ETT has requested from the Minerals Authority to separate the licenses in order to fix this overlap on March 9, 2015 but a decision has still not been made.

Therefore, it is urgent for the authorities to fix this overlap.

14.10 Regarding resource estimates of Tsankhi

According to International JORC standard, Tavantolgoi deposit holds 7.38 billion tons, and the proven reserves are 3.9 billion tons.

The proven reserves for East and West Tsankhi are a combined 2.4 billion tons. This amounts to 60.8% of the total deposits proven reserves. (*Based on ETT information provided to on May 28, 2015 #01/712*).

14.11 Regarding the workforce

The provisions in the April 6, 2015 version of the Investment Agreement that allowed ER to independently hire its workforce, to use its best efforts to hire Mongolian nationals on a competitive basis, and to receive favorable conditions in obtaining the necessary work permits for foreign workers and to get approval on its required quota of foreign workers from the Government have been removed in the April 23, 2015 version.

Articles 5.9 (c) and (d) in the April 23, 2015 version of the Investment Agreement provides that ER will employ Mongolians who fulfill requirements of the job description and if necessary the **Government will assist by establishing the quota for foreign workers in the required amount** for ER, Concession holder, contractors and subcontractors' construction works.

Article 5.9 of the Investment Agreement's "**required amount**" violates Article 43.1 of the Minerals Law, which provides that mineral license holders and its contractors are obliged to provide jobs to Mongolian citizens and no more than 10% of the work force may be comprised of foreign workers. In addition, "required amount" violates 27.4 of the Status of Foreign Nationals Law, which provides that the amount of foreign national residing in Mongolia may not exceed 3% of the total population, and out of this 1 single nationality may not exceed 1%.

The Government must determine the quote within the framework of the law.

14.12 Regarding the Agreement's language and dispute resolution

14.12.1 The Cooperation Agreement's Article 14.5 provides that the agreement shall be prepared in English and Mongolian, and if there are inconsistencies between the two, the English one should prevail.

The Mongolian versions of the draft agreements submitted to Parliament are not official translations, and seem to be translated by some law firm or translation agency. For example, Article 7.1(m) of the Investment Agreement states, "relevant authority that receives instructions or demands from the Government" the wording and phrases do not correspond with the official state language, and proves that it is only translation.

Translated versions of the draft cannot be deemed as official. Parliament cannot accept and have hearings on a draft proposal not reviewed by the Ministry of Foreign Affairs. It should be noted that the Ministry of Foreign Affairs reviewed the Oyu Togloi agreement before being introduced to Parliament for discussion.

Therefore, the relevant officials of the Ministry of Foreign Affairs should review and prepare the Mongolian version of the agreement.

The National Security Council's minutes 24/11 of 2010 provided that the bidding process documents, agreement, and relevant documents for Tavantolgoi deposit should be drafted in Mongolian and English. Mongolian side has to follow this.

We compared the English and Mongolian versions of the Investment Agreement and other related agreements. There are far too many translation mistakes. Two types of mistakes can be identified, (1) mistakes that lead to loss of meaning for provisions and (2) technical and grammatical mistakes.

It is necessary to have official translations of the Investment Agreement and other relevant agreements, thus, English copies were sent to the Ministry of Foreign Affairs for official translation.

14.2.2 Article 26.1(d)(vi) and (g)(ii) provide that the parties agree to the arbitration in London in the event of a dispute and that the Government and its affiliated entities, has waived their current and any future sovereign immunity to jurisdiction in London.

Mongolia became a signatory in 1996 to the Convention on the Settlement of Investment Disputes between States and Nationals of Other States of 1965 ("Convention").

The waiver of sovereign immunity is not required from a state under the Convention. In other words, signatories to the Convention are not obliged to waive their sovereign immunity.

In accordance with the Convention, the Government of Mongolia is not required to waive its jurisdiction, in the event disputes are in connection with the Agreement and other related agreements.

Furthermore, the Government is entering into the Investment Agreement and other related agreements not only with Energy Resources Corporation LLC, but also with China's state owned Shenhua. Disputes over hard set provisions might pose political risks to the good standing relationship with our neighbor. Therefore, we are of the position that these dispute settlement provisions must be reviewed with upmost due diligence.

In sum, the Agreement's official translation must be reviewed and certified by the Ministry of Foreign Affairs.

15. Comments on formula for Reimbursement to be paid by GOM as set forth in Appendix 5 to the Investment Agreement

1. Reimbursement for bank loan will be calculated as sum of product of weighted average annual investment multiplied by debt cost of 12% and a discount rate of 10% for total of X years, from initial investment to contract termination.

$$\sum_{t=1}^{X} AWAII * 12\% * (1 + 10\%)^{X}$$

2. Compensation for loss of revenues to be paid to Investors will be calculated as sum of product of weighted average annual investment multiplied by 15% return on investment, with a discount rate of 10% for total of X years, from initial investment to contract termination.

$$\sum_{t=1}^{X} AWAII * 15\% * (1 + 10\%)^{X}$$

3. If EPC contract is terminated, reimbursement amount to be paid by the GOM will be calculated as total sum of tangible and intangible assets on balance sheet, at the time of the termination, multiplied by 15% return on investment discounted at 10% for n years, from initial investment to contract termination.

$$\sum_{t=1}^{n} \frac{The\ Initial\ value\ of\ T\&I\ assets * 15\%}{(1 + 10\%)\hat{}\, n}$$

For instance, if the GOM decides to terminate the Investment Agreement and Concession Agreement in 1 year, the GOM will be liable to reimburse the Consortium consisting of MMC and Shenhua for an amount of US$51.1 million. If the abovementioned agreements are terminated in 3 years after initial investment the reimbursement will amount to US$409.4 million. Similarly, the reimbursement will be US$966.8 million in 5 years, US$1,467 million in 7 years and US$2,041.3 million in 10 years.

Please see table below for details.

16. Conclusion

The Working Group, established by the Speaker of the Parliament under Order No. 101 of 2015, has worked convened in accordance with the guidelines of the order and hereby submits this conclusion and a draft decision.

16.1 The Investment Agreement and other related agreements prepared in connection with the operation of the Tavantolgoi deposit by Consortium violate the Civil Code, Land Law, Minerals Law, and Railway Transportation Law of Mongolia.

16.2 Government Resolution No. 268 of 2014 which announced the operation of Tavantolgoi Deposit violates Parliament Resolution number 40 dated 12 April 2008,

Article 2.2 of Parliament Resolution No. 32 dated 24 June 2010, Article stating “mining will be done at the Tavantolgoi Deposit jointly with domestic and foreign investors” of Action Plan of the Government of Mongolia for 2012-2016 approved by the Parliament Resolution No. 37 dated 18 September 2012, National Security Council’s Recommendations Number 35/32 of 2011 and 07/04 of 2012 and 04/03 dated 16 February 2015, Government Resolution No. 121 dated 3 November 2012 that granted the license for building railway base structure in the direction of Ukhaa Khudag – Gashuun Sukhait to the “MTZ” JSC, and Government Resolution No 28 dated 26 January 2013 that granted the concession of railway base structure to the “MTZ” JSC respectively.

16.3 The Cooperation Agreement, the Investment Agreement, and Railway Concession Agreement conflict with national security and public interests, do not comply with valid Mongolian legislations, and do not adhere to the business principle of equality and cooperation.

16.4 Appropriate measures have not been taken to protect the rights and to benefit from the 2,558,175,510 shares held by 2,475,201 citizens of Mongolia and 8,497,671 shares held by 553 entities. The Investment Agreement and related agreements fail to address these matters.

The Government failed to implement Article 1.2 of the Parliament’s Petitionary Standing Committee Decree No. 5 dated 18 February 2015, which required the Government to address in the Investment Agreement in a separate provision to protect the rights and economic benefits of the citizens holding 1072 shares in Erdenes Tavantolgoi JSC.

Moreover, on 16 February 2015, the National Security Council issued Recommendation No. 04/03. Article 4 of this Recommendation directed the Government “to involve Erdenes Tavantolgoi JSC’s shares held by the citizens of Mongolia into the economic circulation and to satisfy the condition to obtain dividend from these shares”. However, the Government failed to implement this recommendation.

16.5 Under the Parliament Resolution No. 39 on Operating of “Tavantolgoi Deposit” dated 7 July 2010, measures should be taken for attracting necessary foreign investment by trading up to 20 percent of the shares of Erdenes Tavantolgoi JSC on domestic and international stock exchanges, but no such measures were included in the Investment Agreement and other related agreements. The terms and conditions of the Investment Agreement and Cooperation Agreement are not beneficial to Mongolia; thus, decreasing the value of Erdenes Tavanyolgoi JSC, limiting its operational rights, and blocks the opportunity to float the company’s shares on domestic and international stock exchanges.

16.6 The Government failed to comply with and implement the Annex 1 titled “General principles and guidelines for concluding the investment agreement to jointly operate the Tavantolgoi Coal Deposit” of the Parliament Resolution No. 40 dated 4

December 2008 in drafting and negotiating the Investment Agreement and related agreements with the Consortium.

16.7 The Cooperation Agreement, Investment Agreement, and Railway Concession Agreement for operating the Tavantolgoi deposit fail to satisfy any meaningful participation and investment of "Third Neighbors", and the agreements do not comply with Mongolia's foreign policy principle of "Third Neighbor Policy".

16.8 The construction of the Tavantolgoi deposit's infrastructure and investment methods have low economic benefits to Mongolia. The transfer of the Ukhaa Khudag – Gashuun Sukhait railway to a foreign invested private entity as part of the award of the bidding process violates the National Security Council's Recommendations Number 35/32 of 2011 and 07/04 of 2012, Article 2.2 of the Parliament Resolution No. 32 dated 24 June 2010, which approved the State Railway Policy and Government Resolutions No. 121 dated 3 November 2012 and No. 28 dated 26 January 2013, respectively.

16.9 M.Enkhsaikhan, the Minister of Mongolia, who is leading the working group negotiating on behalf of the Government, directly violates Provision 4 of the Meeting minute of the National Security Council meeting of 18 May 2010. Provision 4 prohibited political officials to participate in any of the negotiations on behalf of any parties". Further, this political official solely made decision and violated the General principles and guidance approved by the Parliament Resolution No. 40 dated 4 December 2008 which provided to involve the assistance of internationally recognized consulting entities to prepare the draft of the Agreement.

As a result, the Government was not in arms-length when negotiating with the Consortium who was consulted by internationally recognized legal and financial firms. Since the abilities of state employees are limited, the working group failed to address many issues that are essential to the interest of the state including due diligence on the investors' financials, on the organizational structure and operational guidelines of the listed foreign investor, and conclusion about the potential effects on the project with regards to international agreements and conventions concluded by Mongolia and the country in which the foreign investor is registered.

16.10 Article 1.4 of the Parliament Resolution No. 34 of 2014 directed that infrastructure matters of the deposit shall be solved through a comprehensive development in an economically viable manner without additionally burdening the state budget, and by satisfying participation of both domestic and foreign investors. However, the Government only solved the Tsankhi Mining development and railway in the direction of Ukhaa Khudag – Gashuun Sukhait, and failed to address railways in other directions such as Tavantolgoi-Sainshand-Huut-Choibalsan-Ereentsav. Moreover, the Government missed to address matters related to mining of deposits licensed to Erdenes Tavan Tolgoi JSC such as Bortolgoi, Borteeg, Oortsog, Onch-Kharaat and involving such fields into economic circulation.

16.11 The competitive bidding was awarded to a legal entity with conflicts of interests by violating Article 1.2 of Government Meeting Minute number 59 dated 17 November 2010. The bidding for the operation of Tavantolgoi Deposit continued among short listed 6 companies, but was awarded to ”Energy Resources Corporation” LLC and its subsidiary “Energy Resource” LLC which were not participants of the bidding.

16.12 “Energy Resources Corporation”, owner of 51% of the Project Company, is 100 percent foreign invested company, and 49% of the Project Company is owned by “China Shenhua Energy”, a foreign legal entity. Therefore, the Tavantolgoi Coal Deposit is effectively being directly and indirectly transferred to the 100% control of foreign entities.

16.13 “Energy Resources Corporation” is owner of 51 percent of the Project Company that won the bid and its shares are pledged in the debt of its parent company the “MMC” Company of the Cayman Islands. Therefore, it is the opinion that “Energy Resources Corporation” is financially incapable to implement the Project. MMC is in financial difficulty. Once it obtains the right to operate the Tavantolgoi Deposit, MMC will have no competitors and will raise its mineral reserves thereby increasing its market valuation. This will enable MMC to withstand its current financial difficulties.

16.14 The total investment in the Project is stated as approximately USD 4 billion and 1 billion of this amount will be considered as ER’s investment made to the Ukhaa Khudag Mining. However, the Agreement lacks any provisions showing what methods or formulas were used to calculate the amount of ER’s investment made to Ukhaa Khudag. MMC is ER’s parent company and owner. MMC’s annual financial statement for 2014 (page number 14 and notes number 23, 25, 26) lists MMC’s total debt at USD 1.285 billion as of 31 December 2014, which includes its long-term and short-term debts.

16.15 It is not clear from the Investment Agreement when and how ER will make the USD 4 billion in investments and how to determine if the investment is made. The Investment Agreement allows ER to split the approximately 4 billion USD of investments over 60 years, which includes the Term of the Agreement 30 years and additional 30 years of extension; ER to reinvest from the income derived from the operation of the Tavantolgoi deposit; or ER to decide the method of investment on its own discretion such as by calculating adding high operations expenses like pre-stripping costs as investments.

16.16 ER will raise investments by creating security interests over its rights and benefits obtained in connection with the operation of the Tavantolgoi deposit. However, this is not an advantage of ER but an opportunity enabled by obtaining the right to operate the Tavantolgoi deposit. Had the Government allowed ETT to have such an opportunity, ETT would have been able to raise financing on its own.

16.17 Under Article 8.4(c)(ii) and 8.4(d)(iv), Financiers shall have right to transfer the object of the Agreement to other entities or to replace Project Company with a third

party with transfer of the relevant rights and obligations to the third party. Therefore, it is the opinion that by including these articles in the Agreement, ER was planning to exit the Investment Agreement and other related agreements in the future in accordance with these articles.

16.18 The translated versions of the draft agreements cannot be deemed as official. Parliament cannot accept and have hearings on a draft proposal not officially reviewed by the Ministry of Foreign Affairs. It should be noted that the Ministry of Foreign Affairs had officially reviewed the Oyu Togloi agreement before being introduced to Parliament for discussion.

16.19 All agreements between the Government and foreign investors with regards to large scale mining projects are followed by certain disputes. Again and again, time has shown that such agreements fail to adequately protect public interests, and the respective officials who were responsible in executing the agreements are never held accountable. This wrong practice repeated itself during the drafting of Tavan Tolgoi agreements.

From the beginning, the Government working group violated existing laws, Parliament resolutions, the National Security Concept, National Security Council's Recommendations and Government Resolutions in negotiating and preparing the draft agreements that are not beneficial to Mongolia with regards to the Tavantolgoi deposit valued at tens of billions of dollars.

Therefore, the relevant politic officials and state employees of the Government working group should be held accountable for their actions as provided under the laws of Mongolia.

16.20 In executing the Investment Agreement and other related agreements, the Government should be obliged to follow its responsibilities in accordance with the Investment Law of Mongolia.

16.21 This Working Group has concluded that both Government Resolutions No. 181 dated 30 May 2012 and No. 268 dated 201 August 2014 should be invalidated.

The invalidation of Government Resolution No. 181 of 2012 will enable the protection of the legal interest of citizens who hold 1072 shares of Erdenes Tavan Tolgoi JSC. The invalidation of Government Resolution No. 268 of 2014 will enable the shortlisted 6 bidders for the operation of Tavantolgoi Deposit to compete again, and the Government will be able to continue and soon finish the bidding process upon the issuance of a new Parliamentary resolution.

16.22 Under Article 3.1 of the Parliament Resolution No. 40 dated 4 December 2008 and Article 1.5 of the Parliament Resolution No. 39 of 2010, the Government should submit the draft agreements for the operation of the Tavantolgoi Coal Deposit for the Parliamentary discussion and resolution.

Therefore, the Parliament should sum up its previous resolutions in connection with the operation the of Tavantolgoi Deposit and issue resolution that includes specific principles and guidelines for the Government to follow. In addition, Parliament should oversee the implementation of this resolution. The Working Group, hereby proposes and submits a draft Parliament Resolution on “the Development of the Tavantolgoi Deposit” to the Parliament. All sources consulted by the Working Group and the draft of the Parliament Resolution are attached.

Leader of the Working Group	L.ERDENECHIMEG (Signed)
	Member of Parliament
Members:	A.BAKEI (Signed)
	Member of Parliament
	Su.BATBOLD (Not signed)
	Member of Parliament
	O.BAASANKHUU (Signed)
	Member of Parliament
	D.GANKHUYAG (Signed)
	Member of Parliament
	S.GANBAATAR (Signed)
	Member of Parliament
	B.NARANKHUU (Signed)
	Member of Parliament
	D.SUMYABAZAR (Signed)
	Member of Parliament
	M.SONOMPIL (Signed)
	Member of Parliament
	B.CHOIJILSUREN (Signed)
	Member of Parliament