5. REVENUE SHARING CASE STUDY: MONGOLIA

Mongolia has enormous natural resource potential and today is a significant producer of copper, gold and coal. On average, from 2006–2011, mineral revenues accounted for 27.6 percent of fiscal revenues, before declining to just over 16 percent from 2012–2014.[32] In a country where local communities are often very small, scattered and impoverished, and there is a general lack of infrastructure or social services, expectations from large mining projects are high. Mining communities often find themselves in direct conflict with companies or the government because of a lack of dialogue and unrealistic expectations around resource-related benefits.

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

Mongolia is a unitary state with a limited degree of fiscal and political decentralization. It is administratively divided into 21 *aimags* (provinces) and 334 *soums* (districts). Both *aimags* and *soums* have elected representatives which constitute local parliaments (Citizens' Representative Khurals).

Most government revenues from the mineral and oil sectors are centralized. While the national government collects all major taxes from the extractive sector, including mineral royalties and corporate income taxes, local governments collect smaller taxes and fees, such as immovable property taxes, land use fees, vehicle taxes, water use fees and royalties on common minerals (gravel and sand). Mineral licences are issued by the national government; however, *aimags* and *soums* are consulted during the licensing process.

In recent years, some efforts have been made toward increasing fiscal decentralization. A key initiative in the decentralization process was the Local Development Fund (LDF) introduced in 2013 and funded partly from mineral royalties.

Due to the decline of mining revenues, the revenues of the LDF have declined substantially in recent years from 195 billion tögrögs (approximately US$108 million) in 2014 to 106 billion tögrögs (approximately US$56 million) in 2015.[33] The decline in mineral revenues has been a significant source of complaint from mining regions. In response, parliament amended the Budget Law, allocating 30 percent of mineral royalties from the locality (excluding royalties from 'large projects of national amplitude') and 50 percent of mining licence fees from the relevant *aimags* and *soums* to the LDFs of those localities. These changes came into effect in January 2016.

Decisions on the uses of LDFs are carried out in a participatory manner. In this way, the LDF spending decision-making process is a significant departure from that used previously in Mongolia. Public discussions are held at each level of administrative unit regarding projects to be funded from an LDF in each locality. These needs are then aggregated and prioritized, and proposals are submitted for financing from the LDFs.

LDFs suffer from several weaknesses, some of which are related to design and others to implementation. In terms of design, considering the insignificant amounts of funds which circulate through the LDFs, they utilize a complex formula for allocation. The funds also do not have clear-cut objectives. Finally, the current allocation formula which uses population size results in a significantly higher level of allocation to the capital city Ulaanbaatar, which is also the wealthiest region. The changes effective as of January 2016 adopt a more derivation-based system of resource revenue sharing, though the design complexity remains.

32. Data for 2006–2011 is from U. Gankhuyag and O. Banzragsh, Extractive industry and the financing of child-inclusive social development in Mongolia (2014). Data for 2012–2014 is from IMF, Mongolia: 2015 Article IV Consultation Staff Report (2015).

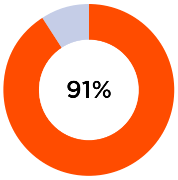
33. Ibid.

MONGOLIA

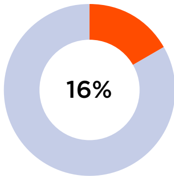
POPULATION (MILLION)**:** 3.0

RESOURCE FOCUS:

Coal, copper and gold



OIL, GAS AND MINING EXPORTS AS A SHARE OF TOTAL EXPORTS



MINERAL REVENUE AS A SHARE OF GOVERNMENT REVENUE

LARGEST MINERAL PRODUCING AIMAGS (2014)

- Orkhon
- Selenge
- Tuv
- Umnugobi

GOVERNMENT

Mongolia is a unitary state administratively divided into 21 aimags (provinces) and 334 soums (districts). Both aimags and soums have elected representatives which constitute local parliaments (Citizens' Representative Khurals).

WHOSE JOB IS IT?

NATIONAL

- Education services
- Health services
- Defense
- Pensions
- Foreign affairs
- Mining
- Energy
- Industrial policy
- National transport infrastructure (e.g. roads, railways)

CITY AND AIMAG

- Urban planning and establishing new infrastructure
- Social care, welfare services and poverty alleviation
- Development of small and medium-sized enterprises
- Water supply, sewerage and drainage systems
- Housing
- Public transport
- Environmental protection and rehabilitation
- Large-scale roads and bridges
- Utilities for public areas, landscaping, public hygiene, street lighting, cleaning, and waste removal
- Maintaining electrical infrastructure

SOUM

- Utilities for public areas, public hygiene, street lighting, cleaning and waste removal
- Protection of nature and the environment
- Public lighting
- Maintenance of sidewalks, recreational areas and children's playgrounds

NATURAL RESOURCE REVENUES

Effective January 2016, mineral producing *aimags* receive:

30% MINERAL ROYALTIES FROM LOCALITY

EXCLUDING ROYALTIES FROM LARGE PROJECTS OF NATIONAL AMPLITUDE

50% MINING LICENSE FEES

NATIONAL

- Corporate income tax
- Value added tax
- Excise tax
- Customs duties
- Fuel and diesel tax
- Mineral royalties
- Mining licence fees
- Air pollution fees
- Water pollution fees
- SOE dividends

CITY AND AIMAG

- Personal income tax
- Land use fees
- Immovable property tax
- Vehicle tax
- Water use fee
- Common minerals royalty
- Income on local property

Sources: World Bank (2015); The Observatory of Economic Complexity (MIT) (2014); IMF (2012-2014 average); Mongolian EITI (2014).