



**NOMIN & ADVOCATES**  
LLP

# **AMENDMENTS TO THE BANKING LAW OF MONGOLIA**

March 2021



## AMENDMENTS TO THE BANKING LAW OF MONGOLIA

The Government of Mongolia's ("**Government**") National Program for the Development of Financial Market of Mongolia<sup>1</sup> and the Monetary Policy of 2020<sup>2</sup> approved by the Parliament of Mongolia's ("**Parliament**") Resolution No. 98, set forth policy goals of strengthening corporate governance of banks, deconcentrating their influential shareholders, and increasing risk tolerance in the banking sector. In line with achieving these goals, the Parliament adopted the Amendments to the Banking Law of Mongolia ("**Amendments**") on 29 January 2021.

The key features of the Amendments include the new requirement for the corporate form of Mongolian commercial banks as well as restrictions on ownership concentration. The Amendments also revised the previous set of rules for determining the insolvency of banks and the order of creditors in the event of liquidation.

On the same date, the Parliament adopted the Law on the Implementation of the Amendments to the Banking Law of Mongolia ("**Implementation Law**"), which sets out the procedural requirements for the implementation of and the compliance with the Amendments.

We summarize below the main changes in the Banking Law of Mongolia enacted by the Amendments.

### 1. CORPORATE FORMS OF BANKS AND MANDATORY IPO

The Amendments introduced a new requirement as to the corporate form of commercial banks operating in Mongolia. All banks operating in Mongolia are currently incorporated as limited liability company. However, pursuant to the Amendments, all commercial banks must be reorganized as joint stock companies under Mongolian law. In particular, the systemically importance banks must be reorganized as open joint stock company, i.e., a public company. The non-systemic banks may be organized as closed joint stock company. Further, the Implementation Law requires banks to comply with this requirement by 30 June 2022.

As a consequence, banks and their activities will be subject to regulations and supervision of both the Bank of Mongolia ("**BoM**") and the Financial Regulatory Commission of Mongolia ("**FRC**"). With respect to mandatory initial public offering of systematically important banks, the details of the requirement, including the possibility of dual listing and issuance of depository receipts, are likely to be regulated in special procedures to be jointly approved by BoM and FRC.

---

<sup>1</sup> <https://www.legalinfo.mn/annex/details/8073?lawid=12935>

<sup>2</sup> <https://www.legalinfo.mn/annex/details/10390?lawid=14893>

### **(a) Definition of Systematically Important Bank**

Before the Amendments, a systematically important bank was defined as a bank which holds 5% or more of the total capital of the Mongolian banking system during the last six months<sup>3</sup>. The Amendments revised and broadened this definition with more multifaceted factors to be considered. A systematically important bank is now defined as bank determined as such by BoM in consideration of the bank's assets, liabilities, its account in the total transaction volume of Mongolia's payment system, core banking operations and its effect on the financial market.

### **(b) Board of Directors**

Following the requirement to reorganize banks from limited liability company to joint stock company, the board of all banks must have no less than 9 directors. Further, the Amendments provide that at least one third of the board members must be independent directors.

In addition, before the Amendments, the board was authorized to appoint the CEO/executive director of the bank in consultation with the President of BoM. Due to uncertainty regarding the level and extent of consultation needed for such appointment, the Amendment expressly provides that the appointment of the executive director is subject to the approval by the President of BoM.

### **(c) Transparency and Reporting**

Furthermore, in connection with the change of corporate forms, commercial banks shall be subject to extended reporting obligations under FRC and applicable stock exchange regulations. For example, in accordance with current FRC regulations applicable to public companies, systemic banks shall have obligations to announce its management decisions that may affect the price of the bank's shares within 1 business day of the decision.

## **2. RESTRICTIONS ON OWNERSHIP CONCENTRATION**

One of the main goals of the Amendments is to deconcentrate the influential shareholders of Mongolian banks for the purpose of strengthening good corporate governance and preventing bank failures due to potential improper influence by large block shareholders.

Accordingly, the Amendments impose 20% shareholding limit per a shareholder, either alone or jointly holding the shares of bank together with its related party. The exception to this requirement applies only to special purpose banks established for the purpose of bank restructuring and to the ownership of the Government in banks recapitalized in accordance with the Law of Mongolia on Ensuring Stability of Banking Sector.

---

<sup>3</sup> Article 4.1.3 of the Law for Ensuring Stability of Banking Sector, enacted on 22 June 2018 (before the enactment of the Amendments)

Further, as previously provided in the Banking Law of Mongolia, the Amendment retains the prohibition for direct or indirect holding of bank shares using another person's name/identity. While the wordings of this provision are relatively broad, in light of the revised definition of influential shareholder in the Amendment, we view that the aim of this prohibition is to prevent circumstances where the ultimate beneficial owner of a bank shareholder intentionally using another person's name to circumvent the requirements of the Banking Law of Mongolia.

The Amendment additionally stipulates that the creation of security interest over bank shares and securities related to shares are prohibited.

The Implementation Law provides that the above restriction on ownership concentration must be complied with by banks by 31 December 2023.

#### **(a) Requirements for Influential Shareholder**

The Amendment broadened the definition of "influential shareholder" to encompass ultimate beneficial owners of any person that holds 5% or more of bank shares alone or together with its related party. The term "influential shareholder" also includes those shareholders who can influence the bank's policy, decisions and management and the ultimate beneficial owners of the same.

Additionally, the Amendments newly provided that an influential shareholder and its ultimate beneficial owner cannot be the President of Mongolia, a member of the Parliament, member of the Cabinet, or other high-ranking public official.

#### **(b) Approval and Notification Regulations**

As provided in the Banking Law of Mongolia, following events, among others, require the prior approval of BoM:

- (a) any issuance of new shares or securities related to shares;
- (b) any changes in the amount and structure of a bank's share capital;
- (c) a person becoming influential shareholder of a bank; and
- (d) redemption of bank shares.

As banks shall be subject to FRC regulations in the light of its corporate forms, the detailed regulations on approval and notification procedures for the above shall be enacted jointly by BoM and FRC.

### **3. INSOLVENCY REGULATIONS FOR BANKS**

The Amendments introduced new set of criteria in respect of determining the insolvency of banks. BoM shall consider a bank to be insolvent or insolvency is imminent in the event of the following:

- (a) a bank fails to pay its depositors, customers or creditors on their first demand, or such inability of payment is determined by bank supervision;
- (b) a bank becomes unable to continue its operations as a result of its incompliance with prudential ratios; or
- (c) a bank's liabilities exceed or will exceed its assets in foreseeable period as determined by bank supervision.

Further, the Amendments revised the ranking of creditors in the event of bank liquidation. The main changes made in the ranking relate to the class of depositors and the type of their accounts held by the liquidated bank. In particular, the Amendment provides that individual non-insured savings and standard accounts receivables are ranked higher than those of legal entities.

#### **4. SANCTIONS AND MEASURES FOR INCOMPLIANCE**

In accordance with the Implementation Law, banks must approve and submit a plan to BoM on implementing the requirements introduced by the Amendments by 1 July 2021. Upon review, BoM in consultation with FRC may demand changes in such plan.

In connection with the above, BoM and FRC are to approve provisional procedures for preparing and implementing the plan.

The Implementation Law also provides that in the event banks fail to comply with the requirements of the Amendment within the timeframes specified in the Implementation Law, BoM is authorized to take a number of measures on the bank and its shareholders such as suspension of voting rights of the influential shareholders, prohibition on dividend payments, appointment of provisional administrator and any other measures available under Mongolian law.

#### **5. CONCLUDING REMARKS**

The Amendments put forward bold measures in respect of how Mongolian banks will be owned and operate that would bring profound changes in the banking sector. For achieving its stated objectives of increasing risk tolerance of banks and strengthening the corporate governance and transparency, it appears to rely on leveraging the capital market force based on adequate transparency of financial activities. However, particularly in respect of systemic banks that are required to become public companies, it remains to be seen how this would affect the banks' management and operational efficiency.

Further, with respect to the limitation on bank shareholdings, we view that while there are good prudential or governance rationale behind dispersed shareholdings, there is a concern regarding the proper implementation and sanctions for the failure to complete by the timeline provided in the law.

\* \* \*

**Nominchimeg Odsuren**

Managing Partner

nominchimeg@nominadvocates.com

+976 7505 3003

**Gal-Ariun Bayaraa**

Associate

gal-ariun@nominadvocates.com

+976 7505 3001

*Disclaimer: This note is prepared solely for the purpose of providing brief and general information to our clients and/or interested persons. This note does not constitute legal advice provided by Nomin & Advocates LLP within the scope of the professional activity of lawyers.*

**NOMIN & ADVOCATES LLP**

Suite 701, Level 7, New Horizons Office

Olympic Street, Sukhbaatar District 1<sup>st</sup> khoroo

Ulaanbaatar 14020, Mongolia

(+976) 7505 3000

[www.nominadvocates.com](http://www.nominadvocates.com)