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Mongolia's Meddling in Mining Operations will Cost it $100 Million

Yancy Cottrill (Staff Attorney at Congress of the Federated States of Micronesia) · Thursday, March 12th, 2015

The Mongolian government has recently been required to pay one Canadian mining company approximately $100 million for expropriating that company's uranium extraction licences in 2009. This sum is payable to Khan Resources Inc (Khan) pursuant to an arbitral award that is the climax of an arbitration proceeding initiated by Khan in 2011 as a result of the Mongolian government's alleged interference in its mining operations (*Khan Resources Inc, Khan Resources BV and Cauc Holding Company Ltd v Government of Mongolia*, UNCITRAL).

The facts

Khan took over the Dornod uranium deposit sometime after 1995 from Russia's Priargunsky Mining & Chemical Enterprise. Khan released a feasibility study in March 2009 which showed that the project was viable. Shortly afterwards, in July, the Mongolian government passed the Nuclear Energy Law (2009), which gave 51% ownership of the operation to the state without compensation to Khan.

Moreover, in February 2010 the Mongolian government suspended and then cancelled Khan's mining licences. This expropriation took place immediately after Khan had recommended to its shareholders that they accept a full takeover of the company by China National Nuclear Corporation (CNNC), which is owned by the Chinese government.

The dispute

The ad hoc arbitral tribunal (Tribunal), which had been constituted under the UNCITRAL Arbitration Rules, held that the Mongolian government's actions were in violation of the previous Mongolian Foreign Investment Law (1993) and, as a result, breached the multilateral Energy Charter Treaty (1994). Mongolia is a Contracting State to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards (1958). Khan officials have stated in an official press release on the award that they would initiate collection proceedings if payment of the amount awarded were not forthcoming.

The Tribunal awarded Khan less than half of its original claim of $354 million. It relied on CNNC's 2010 bid in arriving at an appropriate value for the Dornod asset in 2009, which was $80 million. It also awarded interest from the date of the award until payment. Finally, Khan received full arbitration and counsel costs amounting to $9.1 million.

The announcement of this award by Khan on 2 March 2015 came just days after thousands of Mongolians had gathered on Chinggis Square in Ulaanbaatar to protest against mining operations at Noyon Mountain and amendments to another mining law aimed at resource conservation. Mongolian citizens are keenly aware of their country's resources and the efforts of the government both to exploit and conserve them. By way of background, it may be noted that Mongolia broadcast live, on prime time television, a parliamentary debate regarding the particulars of another mining contract.

No doubt the Mongolian people will take note of this arbitral award. It will serve as a wake-up call to the government that it must adhere to its own laws, abide by international treaties and curb the desire to expropriate assets without proper compensation. Foreign investors will closely follow Mongolia's willingness to show adherence to the rule of law by paying the award.

Grant Edey, President and CEO of Khan, stated in the company's press release:

> "A former Mongolian government illegally expropriated Khan's uranium property without any compensation[,] which is contrary to the rule of law. And while the Mongolian government has taken certain progressive action to diminish the harmful acts of former regimes, western investors and governments will scrutinize the Mongolian government's action in this matter as [the] rule of law also dictates prompt payment of compensation."

The Mongolian government has in recent years taken some surprising actions against foreign investors. Besides the much-publicised dispute between the government and Rio Tinto, an Australian mining company, over the Oyu Tolgoi copper and gold deposits, previous governments have passed restrictive foreign investment laws and cancelled mining licences, resulting in a sharp decline in foreign direct investment (FDI). The country's central bank reported last autumn a 70% drop in FDI in the 2014 fiscal year, coming on the heels of a 47% decrease in the 2013 fiscal year.

Only a few years ago, Mongolia's economy was riding high on a wave of foreign investment spurred on by the mining industry. As evidenced by the government's actions against Khan, however, the country's attitude towards foreign companies has been inimical. Prompt payment of the Khan arbitral award should reassure foreign investors that the new government is serious about both upholding the rule of law and attracting FDI to the mineral-rich nation. It should also be noted that the Foreign Investment Law (1993) has been superseded by the Foreign Investment Law (2013), the aim of which is to ease restrictions on foreign investors.

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This entry was posted on Thursday, March 12th, 2015 at 12:01 am and is filed under Energy Charter Treaty, Expropriation, Foreign Investment Law, Investment Arbitration
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