Current Circumstances of Corporate Governance of Mongolian Joint-stock Companies

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Mongolia, a country encountering a new development era, feels a strong need to thoroughly study corporate governance issues particularly corporate ethics, social responsibility, finance, Board of Directors, executive management and environmental performance followed by identifying new development trends of corporate governance.

Companies with multiple owners often encounter governance related issues directly. Business entities in Mongolia are classified into several basic types including LLC, joint-stock company, partnership and cooperative. According to Mongolian legislation, joint-stock companies are subject to listing on stock exchange. Currently, 335 joint-stock companies are listed on Mongolian Stock Exchange, of which 22 are partly owned by the state. According to statistics of MSE, only 140 companies are regularly releasing their reports; means that these companies are operating active.

A team of Japanese and Mongolian researchers of us conducted a corporate governance survey focusing on Mongolia's joint-stock companies and respective findings are described below.

Team of researchers conducted a questionnaire survey among 100 active joint-stock companies with assistance from D.Dugerjav, Deputy Chair of Financial Regulatory Committee. The respondent companies represent 71.4% of active companies on the market. The survey was first-of-its-kind survey conducted in Mongolia on corporate governance issues.

The survey aimed at analyzing general data and indicators of MSE registered joint-stock companies, identifying peculiarities of their Board of Directors, its structure and executive management schemes followed by defining scope and level of corporate impact on environment and measures taken to mitigate the impacts.

At the outset of questionnaire, survey team requested all Chairman or members of Board of Directors or executive managers to personally fill out the questionnaire. Upon checking filled out questionnaire, the team found that 83.4% of questionnaires were filled directly by Chairman or a member or Board of Directors or executive manager greatly reducing the likelihoods of error in surveying (Fig. 1).

Respondent companies mainly operate in the field of electric and thermal power production, water supply, mining, real estate development and lease, extractive industry, hotel, transportation, crop planting, retail and wholesale trading, logistics and warehousing. The survey identified that majority of companies are operating real estate development & lease and retail & wholesale

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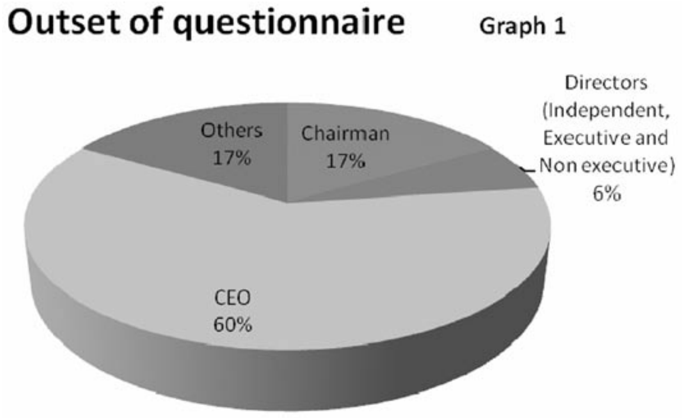

Fig. 1.

trading; transportation, warehousing, electric and thermal power production, construction and water supply companies were the runner-ups.

Of companies, 64.9% employ less than 100 staff showing many of them operate in field that is less intensive in terms of human resource.

Since People's Revolution in 1921, new industrial sectors like light industry and agriculture have emerged and rapidly developed in Mongolia. Throughout the history since that time, businesses have gone through different types of ownership until the country shifted from centrally planned economy to market economy in 1990. The survey unveiled that more than 20 companies operated before 1990, then later shifted to joint-stock company type as a result of privatization. Remaining companies were established and listed at MSE after country's transition to market economy. However, 76.5% of companies are operating more than 10 years with listing at MSE prior to 2001 demonstrating that fewer companies have gone public for last decade. On the other hand, most companies have operated for quite a long time.

Mongolia's Company Law, which was in effect until recently (amended on 6 October 2011), requires members of Board of Directors to be 9 of more. Conversely, our survey identified that 13 companies have 8 or less members in their Board of Directors. 78 companies have their Boards consisting of non-executive members, of which 67.6% have 5–8 non-executive members. Dominating structures in the Boards of open companies generally consist of representatives of shareholders, of which one acts as CEO while the remaining members are non-executive members.

Survey findings show that control on the control package increase as number of Board members increase, while percentage of family members is dropping. Company Law requires at least 9 members; however some companies do not know about the provision and Financial Regulatory Committee and MSE, the institutions tasked to oversee the enforcement, often fail in ensuring the compliance with legal obligations.

An interesting finding was that percentage of family ownership is either high or almost zero. 57.7% of surveyed companies have independent members in their Board of Directors of which 87.4% have up to 6 independent board members.

24.5% of respondent companies have no by-laws of Board of Directors showing incomplete formulation of basic documents necessary for good corporate governance and showcasing inappropriate operation of the Board. 4 companies have had no Board meeting throughout the year; possibly these companies are managed by not the Board, but by other bodies. 59.6% of all respondents organize its Board meeting only 1–4 times a year.

Half of Board Members are not paid while remaining half receives salaries and bonuses on top of dividends. But the amount of their remuneration is relatively low, up to MNT 400000.

83.7% of respondent companies are pure private without any government owned stake showing very little discrepancy with national statistics.

In terms of the respondent companies, 70% of them have their control package owned by family based businesses. Of 56 companies organizing their Board meeting 1-4 times a year, have a family based ownership; means that their control package is owned by families. For 30% companies organizing their Board meeting 5-7 times a year, their control package is owned by families. This clearly demonstrates that the less the family ownership, the more the meeting are.

Of families that own control package of shares, 23% do not participate in executive management, while 40% of the remaining 77% work as a Chairman of Board, 49% work as CEO and the remaining work as Board members. On two companies, one person works as a Board Chairman and CEO simultaneously.

48% or half of the companies have not formalized their mission statement while only 32.3% is in the process of developing their business ethics code.

The team also studied the adverse environmental impacts of respondent companies using 8 indicators including impact on air quality, water quality, soil, land deterioration, noise, vibration, odor and other. Half of the respondents, even more than half, still fail in mitigating their adverse impact on the environment. In addition, 21% are not aware of the environment related legislations.

Survey was conducted on identifying current actions to resolve/mitigate the environment related issues using the following 9 indicators:

1) Environmentally friendly operations
2) Environmentally friendly produce and processing
3) Mitigating the use of natural resources
4) Use of natural power (renewable)
5) Use of recyclable materials
6) Use of secondary raw materials
7) Energy efficiency
8) Environment training for the staff
9) Waste management and recycling

75% of the respondent companies were found not paying attention to these aforementioned indicators for their environmental performance.

The survey shows that the existing government policy does not encourage companies to be environmentally friendly and have better environmental performance.

28 companies equal to 30.4% do not spend funds for environment protection and conservation, which is worth mentioning. In other words, 71.7% do not spend at all or allocate very limited amount for this purpose less than MNT 3 million, which is too low compared to their revenues.

Conclusion

The key operation areas of shareholding companies are relative low showing that so many untapped opportunities exist in Mongolia. Companies differ from each other in terms of size, but both types of companies have fewer staff.

Many companies violate legislation stating that the number of Board members should be 8 or more.

Most of the companies have no by-laws of Board of Directors showing incomplete formulation of basic documents necessary for good corporate governance and showcasing inappropriate operation of the Board.

There is no any tangible and virtual role of non-executive and independent directors. The government policy also does not encourage the companies to run environmentally sound and friendly operations.

Half of the companies have not formalized their mission statement while only few are in the process of developing their business ethics code.

Half of the respondents, even more than half, still fail in mitigating their adverse impact on the environment. Majority of the respondent companies were found not paying attention to the aforementioned indicators for their environmental performance.

The survey shows that the existing government policy does not encourage companies to be environmentally friendly and have better environmental performance.

These conclusions are based on findings of the survey; however many other activities and survey are underway including other surveys, detailed assessments, legal review, information dissemination on the good corporate governance and creating sound and open stock market etc targeted on reforms and improvement of corporate governance.