

MONGOLIA
RESOLUTION OF FINANCIAL REGULATORY COMMISSION

July 7th 2008

No.185

Ulaanbaatar city

Re: Temporary regulation on provision of venture capital by the Non-banking financial institution

Pursuant to provisions 6.1.2 of the law on FRC's legal status, FRC is RESOLVED as follows:

1. Approve the Temporary regulation on provision of venture capital by the Non-banking financial institution as attachment 1, and the report on investment as attachment 2.
2. Assign the duty to the Board of Directors and Chief Executive Officer of the Non-banking financial institution that is authorised to engage in venture capital services to draft and approve the regulation on provision of venture capital services consistent with its operational nature and submit the copy to FRC.
3. Assign the duty to Microfinance Department (N.Oyunchimeg) to ensure advocating, implementation and monitoring of the regulation and Executive office (N.Udaanjargal) to ensure public disclosure.

Chairman

D.Bayarsaikhan

Copy is true:

Head of Executive office

O.Ganbat

**TEMPORARY REGULATION ON PROVISION OF VENTURE CAPITAL BY
NON-BANKING FINANCIAL INSTITUTION**

ONE. GENERAL PROVISIONS

- 1.1 The purpose of this regulation is to regulate the relations that may arise out of supporting the proposal and initiatives to adopt new financial services introduced by Non-banking financial institutions (hereinafter referred to “NBFI”) through Financial Regulatory Commission’s (hereinafter referred to “Commission”) policy, protecting the rights and interests of the investors and clients, preventing from potential risks and undertaking oversight.
- 1.2 The services for provision of venture capital shall be delivered to a legal entity (NBFI), who has been issued a license to engage in non-banking financial services by the Commission and who has been applied for rendering this service and to this extent has been granted a license accordingly.
- 1.3 The issuance of license to deliver services for venture capital and other regulations shall be resolved in accordance with the “Regulation on issuing license to engage in non-banking financial services”.

TWO. DEFINITIONS

- 2.1 “Services of Venture capital” is a financial service to make investment from its (NBFI) equity to hold certain parts of its client-limited liability company (hereinafter referred to “Company”)’s shares for the contractual term under the investment contract and undertake financial management;
- 2.2 “Investment contract” is a written agreement executed by and between the NBFI and the Company under the Article 406 of the Civil Code and this regulation.
- 2.3 “Investor” is a NBFI who has a license to engage in non-banking financial services and has been granted a license to deliver services of venture capital and makes an investment from its paid-in-capital into the limited liability company for a definite period;
- 2.4 “Client company” is a company who authorized to make an investment into its paid-in-capital through allowing to hold its certain shares for a contractual term.

THREE. RIGHTS AND OBLIGATIONS OF NBFI

- 3.1 NBFI to be engaged in services of venture capital shall exercise the following rights:

- 3.1.1 Review the business, financial and other required information of a company that has requested to have services of venture capital;
 - 3.1.2 Conduct due diligence on management capacity, business plan and business operations of a client company and make a decision on investment;
 - 3.1.3 Make investment into the paid-in-capital of a client company upon holding shares for an indefinite period;
 - 3.1.4 Ensure supervision on the operations of a client company from the effective date of investment contract and request relevant reports and records;
 - 3.1.5 Get profit /benefit/ as agreed under the investment contract;
 - 3.1.6 Propose to amend, make changes and terminate the investment contract;
 - 3.1.7 Lodge claim with the court with respect to any dispute that has arisen out of investment contract;
 - 3.1.8 Other rights as assigned by legislation;
- 3.2 NBFi to be engaged in services of venture capital shall have the following duties:
- 3.2.1 NBFi wishes to engage in services of venture capital shall compile and submit to FRC the required documents in accordance with provision 5.2 of the “Regulation on issuing license to engage in non-banking financial services”.
 - 3.2.2 Assign the assets described in the investment contract to the client company;
 - 3.2.3 NBFi with a license to engage in non-banking financial services shall engage in services of venture capital in association with non-banking financial services;
 - 3.2.4 NBFi shall draft and approve the regulation on rendering services of venture capital and submit a copy to the Commission.
 - 3.2.5 Ensure requirements of prudential ratio set forth by the Commission, on a regular basis;
 - 3.2.6 NBFi with a license to render services of venture capital shall submit its monthly financial prudential ratio and investment reports within 10th day of the following month.
 - 3.2.7 Ensure appropriate system that is set to ensure management of investment risks and supervision.

FOUR. REQUIREMENTS FOR ENGAGEMENT OF RENDERING SERVICES OF VENTURE CAPITAL

- 4.1 The following requirements shall be observed when engaged in rendering services of venture capital.
 - 4.1.1 NBFi shall be engaged in rendering services of venture capital upon obtaining the license from the Commission;

- 4.1.2 The amount of paid-in-capital of the NBFI, to be engaged in rendering services of venture capital, shall be not less than MNT 1,000,000,000 (one billion).
- 4.1.3 The term for services of venture capital shall be not less than 2 years.
- 4.1.4 The total investment shall not be more than 50 percent of NBFI's equity.
- 4.1.5 NBFI that is engaged in services of venture capital shall hold not more than 49 percent of a client company's shares.
- 4.1.6 The prudential ratios set by the Commission shall be met fully.
- 4.1.7 NBFI, an investor, may insure its capital invested.
- 4.1.8 Based upon the request of NBFI with a license to engage in non-banking financial services, the issuance of license to engage in rendering services of venture capital shall be resolved at the Commission's meeting.
- 4.1.9 NBFI shall open and maintain the file for each client company, that has received services of venture capital. The general investment contract, company's charter, company's management and internal procedures and regulations, and other documents related to investment shall be attached to the file.

FIVE. PROHIBITIONS FOR RENDERING SERVICES OF VENTURE CAPITAL

- 5.1 The following actions shall be prohibited while being engaged in rendering services of venture capital:
 - 5.1.1 Make false and incorrect statement and advocacy on services of venture capital;
 - 5.1.2 The term of services of venture capital is not defined;
 - 5.1.3 Use sources of cash, which is not reflected in the financial statement of a NBFI, for venture capital purpose;
 - 5.1.4 Make investment using the mobilized funds;
 - 5.1.5 Engage in rendering services of venture capital without a license obtained from the Commission;
 - 5.1.6 The Client company uses the venture capital for the purposes other than the investment contract;

SIX. EXECUTION AND TERMINATION OF INVESTMENT CONTRACT

- 6.1 The investment contract shall be executed upon bilateral agreement by NBFI that has been granted the license to render the services of venture capital and the client company.
- 6.2 The investment contract shall be executed in writing in accordance with Article 406 of the Civil Code.
- 6.3 The investment contract must reflect the following:

- 6.3.1 i.e name, address, telephone number, certificate number, proxy of parties to the contract,
- 6.3.2 General term and phases;
- 6.3.3 Total investment and schedule for investment;
- 6.3.4 Rights, duties and obligations of parties;
- 6.3.5 General principles reflected in the Company's charter i.e management, regulation, monitoring system, power of authority;
- 6.3.6 Repayment form, conditions and procedures (i.e Company buys-back its shares, assign its shares to a third party, public offering);
- 6.3.7 Reporting period and form of progress report to be obtained;
- 6.3.8 Conditions, needs and regulation on additional venture capital;
- 6.3.9 Dividends and other profits, benefits and principles on distribution;
- 6.3.10 Rights and obligations of parties with respect to prevention of risks;
- 6.3.11 Conditions and requirements for monitoring the implementation of contract;
- 6.3.12 Principles on regulating changes to management, structure and amendment to company's charter;
- 6.3.13 Conclude the performance, consequence and regulation;
- 6.3.14 Circumstances for termination of contract.

SEVEN. MONITORING ON SERVICES OF VENTURE CAPITAL

- 7.1 The investor (NBFI) shall oversee if the venture capital is used in compliance with legislation and investment contract.
- 7.2 The Commission shall monitor if the NBFI, engaged in rendering services of venture capital, is meeting the prudential ratio requirements through its monthly reports and when required shall make site visits and take required measures.

EIGHT. LIABILITY

- 8.1 The Commission shall take the following measures, if the NBFI, engaged in rendering services of venture capital, is found to be not meeting the prudential ratio requirements and requirements set forth in this regulation, and circumstances for potential exposure to risks is established. These are:
 - 8.1.1 Request NBFI to increase its equity;
 - 8.1.2 Prohibit to make additional investment into the services of venture capital;
 - 8.1.3 Suspend the license to engage in rendering services of venture capital;
 - 8.1.4 Revoke the license to engage in rendering services of venture capital;
- 8.2 If the violation of this regulation, while rendering the services of venture capital is not subject to criminal offense, then it will be subject to administrative liabilities under the legislation.

- 8.2 Any dispute that has arisen in connection with services of venture capital shall be resolved by competent authority based on investment contract and applicable legislation.

FINANCIAL REGULATORY COMMISSION