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BREIF: LAW OF MONGOLIA ON MOVABLE AND INTANGIBLE PROPERTY PLEDGES

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The Mongolian Parliament approved the Law of Mongolia on Movable and Intangible Property Pledges (the "MIPP Law") and the accompanying Law of Mongolia on the Implementation of the MIPP Law (the "Implementation Law") on July 02, 2015. The MIPP Law and the Implementation Law will come into force on the first of September 2016. The effects of the Implementation Law will be retroactive from that date, meaning that the law will apply to pledge agreements executed prior to September 1, 2016.

The Law is intended to clarify the legal framework governing pledges of “moveable and intangible” properties. In other words, non real estate, or otherwise non-fixed properties as well as property rights and interests created by law. As defined in the MIPP Law itself, this will include existing or future properties capable of transfer, and specifically, all types of shares, securities, claims, all types of scientific, literary, and cultural works, inventions, industrial designs and models, trademarks, utility models, and other movable and intangible property. The law also covers cash, and bank accounts.

A pledge may be created either by way of written agreement between the interested parties or by operation of law. Pledge agreements must be executed in written form and must contain certain mandatory provisions as outlined in the MIPP law. The pledge agreement creates a security interest over specified collateral between a pledgee and a pledgor.



The pledgor is the party with current possession or control over the collateral. In creating the pledge, the pledgor promises by written contract to transfer the collateral to the pledgee under specified conditions. The pledge is a security over the collateral, typically created when the pledgor has received a loan or other credit from the pledgee. A properly executed and perfected pledge gives the pledgee a priority security interest over the collateral enabling the pledgee to recover before other creditors.

A MODERN REGISTRATION MECHANISM

The MIPP Law mandates the General Authority for State Registration ("SRA") to create an electronic registration system for security interests over movable and intangible property ("Pledge Registry"). The MIPP law introduces a new electronic registration and notice system. Under the new registration system, a security interest is registered online with the registry. A the registration notice must contain certain vital information in connection with the security interest including the names and addresses of the parties, the security period, and description of the pledged collateral.

It is expected that the new registration will make registration easier and faster, and will reduce the need for paper documentation. The Pledge Registry will not verify the legality of the underlying transaction or security interest.

Under the MIPP, the pledgee is responsible for registration; however written approval of the pledgor is required. The parties are free to extend, alter or de-register the security interest as they see fit, however any changes should be re-registered via the online system. It is intended that the Pledge Registry will be accessible to the public through an online search function administered by the SRA.

Interestingly, the MIPP Law allows notice of security interest to be registered prior to the execution of a Pledge Agreement. Registration in advance will provide additional comfort to creditors that no higher priority security interest in respect of particular collateral may be registered over the course of finalizing a Pledge Agreement.



PERFECTING A PLEDGE

Under the Law, valid Pledges may be perfected in two potential ways. Firstly, a pledge may be perfected by the transfer of the pledged collateral to the pledgee's possession.

Alternatively, if collateral is not transferred to the pledgee's possession, the pledge may be perfected by registering the security interest with the Pledge Registry. The Pledge Registry serves as notice to the public of the security interest in the collateral. Pledges seeking to perfect their pledge must register. The registration system is available for pledges created by agreement or for pledges created by function of the law.

Pledges created prior to September 01, 2016 may be registered and perfected within a six month period from that date.

Claims of secured creditors such as pledgees shall be ranked and prioritized in the chronological order of their date and time of pledge perfection. However, perfected security interests shall have priority over non-perfected security interests irrespective of the date the security interest was first created.

For several unperfected pledges, the date of creation of the security interest will determine order of priority. If no pledgee has registered their security interest, the pledgee with the oldest pledge will have priority.

PLEDGE ENFORCEMENT

Unless otherwise stated by agreement, if a pledgor has failed to perform its obligations, a pledgee shall be entitled to enforce its secured interest. If grounds for enforcement of security interest are met, the pledgee shall notify the pledgor in writing. If grounds for enforcement include default on the pledgee's obligations under a pledge agreement, the pledgee must issue a notice to the pledgor requesting remedy. The pledgor is then allowed a period of no less than 14 days in which to remedy the default. If the pledgor is unable to remedy the default, the pledgee may



proceed to enforce the pledge. The enforcement action must be reported to the Pledge Registry.

The MIPP Law provides simplified and expedited procedures legal proceedings to enforce a pledge. For example, under the new regime, a pledgee may demand possession of the pledged collateral from the pledgors in the event of enforcement. If such request is not complied with, the pledgee may file a claim at court requesting issue of an order for possession within seven days of submission of the claim.

In terms of methods to dispose of secured collateral and recover cash obligations owed, the MIPP law provides for three options: direct sale, auction or market sale. In any event, the MIPP Law obliges the pledgee to choose the most cost-efficient method. Certain types of security interests, such as pledges over bank accounts and certain securities, may be enforced without undertaking judicial proceedings.

Parties may insure collateral upon contractual basis. If the insured event occurs, pledgee shall be entitled to demand satisfaction from insurance compensation.

OUTLOOK

Implementation of the MIPP Law is a positive step for Mongolia and for domestic and international lenders. Pledges over these movable and intangible properties were possible previously, but the law did not effectively address issues such as identification of collateral, perfection and registration. The new law is a big improvement providing both lenders and borrowers clarity regarding what properties may be pledged, and how to effectively secure the collateral. The Pledge Registry in particular will make searches and verification of existing securities much easier, giving lenders more confidence in providing loans over collateral which they now have the ability to be sure is free from other security interests.