ENVIRONMENTAL, SOCIAL, AND GOVERNANCE (ESG), ITS LEGAL REGULATION

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LEGAL ALERT: ENVIRONMENTAL, SOCIAL, AND GOVERNANCE (ESG), ITS LEGAL REGULATION

The Financial Regulatory Commission of Mongolia ("FRC") approved the revision of the Corporate Governance Code ("Code") on March 23, 2022. Additionally, in August 2022, the FRC established Environmental, Social, and Governance (ESG) or sustainability reporting standards and guidance documents ("Guidelines"). These initiatives aim to enhance the transparency of companies registered in the Mongolian stock market, issuers considering registration in the future, and organizations seeking to improve their reporting practices. In other words, the FRC suggests that even unlisted organizations can utilize the Guidelines for evaluating their sustainability reporting status, as well as identifying and addressing any issues.

In recent years, the credibility of an organization's long-term success has been increasingly evaluated based on the positive impacts it generates within the framework of ESG principles. Moreover, investors are increasingly utilizing ESG criteria to assess a company's social and environmental impact before investing.

ESG, and its importance

Long-term financial performance

Considering ESG indicators is becoming common practice when seeking financial resources or securing loans, the European Bank for Reconstruction and Development takes into account green projects or environmental friendliness when assessing loan eligibility.

The reputation of the organization

Adhering to ESG principles allows an organization to showcase its dedication to sustainability, social responsibility, and ethical business conduct, ultimately bolstering its reputation. Consequently, the brand's overall reputation can experience a boost, along with increased trust from loyal customers and investors.

Risk management

It assists companies in risk mitigation by identifying potential ESG issues before they escalate into significant challenges.

Increase competitiveness

Companies gain a competitive advantage by attracting environmentally friendly customers. Because consumers and customers are willing to pay more for eco-friendly products.

Examples of ESG criteria

Environmental

- Climate change
- Loss of biodiversity

- Waste and pollution
- Energy efficiency

Social

- Human rights
- Employment condition
- Occupational safety and health
- Confidentiality and Data Protection
- Customer satisfaction

Governance

- Tax Strategy
- Corruption and bribery
- Business ethics
- Board diversity

Internationally recognized reporting methods and standards

Guidelines/Methodology	Purpose	Benefit
UN Global Compact	Adhering to the 10 principles of the UN Sustainable Development Goals, companies are committed to annually reporting on their sustainability performance and progress.	This results in an obligation to adhere to a wide range of international norms. It is a comprehensive and flexible methodology suitable for developing markets and small companies.
International Organization for Standardization	It aims to expand external relations for maximizing contribution to sustainable development and improving social responsibility performance.	It provides flexibility for reporting entities to report in accordance with international best practices. Moreover, it is a comprehensive and flexible methodology suitable for developing markets and small companies.
Global Reporting Initiative	It aims to improve the organization's sustainability, support sustainable development, and develop	It covers issues relevant to emerging markets and promotes a wide range of sustainability or non-financial

	the Guidelines with the participation of stakeholders.	management issues to diverse stakeholders.
Integrated Reporting	It aims to increase the long-term holistic thinking of companies and improve the allocation of financial assets. While the report serves all stakeholders, its significance is particularly pronounced for investors.	It is well-suited for developing markets and valuable for reporting on value creation processes, as well as for explaining the strategic management of sustainability issues.

What to report?

The reporting model adopted by the ESG aligns with international reporting methodologies and standards. It outlines 30 key indicators that must be reported, serving as the baseline for reporting requirements.

Types	Code	Reporting issues
Sustainability management system indicators	MS1	Leadership management and commitment
	MS2	Sustainability policy and regulation
	MS3	Management structure
	MS4	Sustainable Development Impact Assessment
	MS5	Capacity building
	MS6	Control analysis
	MS7	Sustainability reporting and verification
	MS8	Membership
Environmental indicators	E1	Energy
	E2	Greenhouse gas emissions
	E3	Climate change
	E4	Water
	E5	Waste

	E6	Biodiversity
Social indicators	S1	Human resource development
	S2	Occupational safety and health
	S3	Equality
	S4	Accessible environment and participation
	S5	Social responsibility and transparency
	S6	Sustainable Supply Chain Management
Governance indicators	G1	Company governance
	G2	Corruption, ethics
	G3	Compliance/Enforcement
	G4	Stakeholder engagement
Additional Industry Indicators	FS	Financial services
	A	Agriculture and food production
	T	Textile industry
	MA	Processing industry
	MI	Mining
	CO	Construction

How to report?

Companies can benefit from following the steps outlined below to establish an efficient and effective reporting system. These steps include:

1. Top management decisions
2. Appoint a responsible person
3. Identify material issues
4. Define indicators
5. Develop reporting plans and relevant information
6. Issuance of warrants
7. Report development and reporting
8. Continuous improvement plan

Responsibility

According to the principles outlined in the Code, the company's Board of Directors (BoD) is responsible for ensuring the accuracy, completeness, and balance of both financial and non-financial reporting and information disclosure. Furthermore, the BoD is required to publish the governance documents, rules, regulations, and instructions outlined in this Code on its website for public access. It is mandated that non-financial reporting should encompass information that assesses the factors and risks impacting the company's sustainable operations across environmental, social, and economic areas, as well as the achievements of the company's goals and objectives. The FRC has mandated that ***public joint-stock companies***, ***insurers***, and ***companies engaged in non-bank financial trust services*** and ***investment management activities*** adhere to the Code, with other companies strongly recommended to do the same, and companies that fail to comply with the Code shall be fined 20,000,000 MNT according to the Law on Violations.

Legal sources:

1. Environmental, Social, and Governance (ESG) or sustainability reporting standards and guidance documents, 2022
2. Corporate Governance Code, 2022
3. Law on Violations, 2017

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