



January 17, 2018

Dear Ms. Ahlers,

Thank you for your letter dated December 22, 2017 and the draft report of SOMO's research into the Oyu Tolgoi ("OT") mine project in Mongolia. Your desire to publish accurate information about the project is appreciated.

OT and its investors are committed to tax transparency. We believe that our tax practices are not only compliant with local laws, international standards and voluntary commitments, but that the OT operation is substantially contributing to Mongolia's economy and long term development. To illustrate this point:

- OT is the largest private sector employer in the country with over 13,000 employees and contractors (94% being Mongolian nationals).<sup>1</sup>
- Despite its early stages of development, OT has paid since 2010 approximately US\$1.7 billion in the form of taxes (VAT, customs, social security and withholding) and royalties and is the country's top corporate taxpayer.<sup>2</sup>
- By the time the underground project begins production around mid-2020, shareholders will have invested approximately US\$12 billion<sup>3</sup> in developing the open pit and the underground project. To that end, it should be noted that the Government of Mongolia (GoM) is the only shareholder that has received a return to date, in the form of taxes and royalties.
- Between 2010 and Q3'17, OT has spent US\$6.7 billion<sup>4</sup> in Mongolia, which includes salaries, payments to Mongolian suppliers, taxes and other payments to the GoM.

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<sup>1</sup> <http://ot.mn/scorecard/>

<sup>2</sup> [http://www.riotinto.com/documents/RT\\_taxes\\_paid\\_in\\_2016.pdf](http://www.riotinto.com/documents/RT_taxes_paid_in_2016.pdf)

<sup>3</sup> [http://www.riotinto.com/media/media-releases-237\\_17323.aspx](http://www.riotinto.com/media/media-releases-237_17323.aspx)

<sup>4</sup> <http://ot.mn/scorecard/>

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- OT is significantly contributing to Mongolia's growth, transacting with 642 domestic suppliers<sup>5</sup> and partners and spending approximately US\$1 billion from January through end of September 2017 with national suppliers for both operational and developmental activities.

We do not agree with the allegation in the report of abusive tax practices, including the implications that OT is not paying its fair share of tax or that the financing structures are in some way reducing tax revenue to the GoM. Nor do we agree with the incorrect assertions made relating to OT's safety performance and community contribution.

The contracts that stabilize the terms of investment in OT have been agreed to by all parties based on a transparent set of facts and on terms commensurate with mining operations in other global locations.

We believe a significant number of the statements presented as alleged facts in the SOMO report are inaccurate or unsubstantiated. We have outlined our comments in two appendices to this letter which cover both our high level concerns and our specific comments on key sections we do not agree with and are factually incorrect. Due to the volume of inaccurate statements in the report, we have not responded to every single point.

Of note, we request that section 3.3 of the SOMO report be deleted. This section irresponsibly and unquestionably repeats speculative assertions that have been firmly denied by Mr Bayartsogt. Insofar as allegations are made against Rio Tinto or Turquoise Hill, they are entirely untrue and there is no evidence to support them. The publication of section 3.3 is likely to cause serious harm to the reputation of Rio Tinto and Turquoise Hill Resources, it is defamatory. We also note that by publishing section 3.3, SOMO would breach its own Code of Conduct for research, including paragraph 3 ("Reliability"). Please confirm immediately that section 3.3 will be deleted from any further versions of the report.

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<sup>5</sup> <http://ot.mn/scorecard/>



Section 3.3 notwithstanding, we suggest that the clarifications expressed in both appendices to this letter be taken into account and your report revised accordingly.

### **Conclusion**

We have made a firm commitment to delivering long-term value at OT. We believe that the current fiscal arrangements, together with our broader economic and community contributions, will achieve this goal. We once again, offer the SOMO team an opportunity to discuss our response with our tax experts.

Thank you for the opportunity to respond to your report and we request that this letter along with the appendices be published within your report.

Yours sincerely,

Luke Colton  
Chief Financial Officer  
Turquoise Hill Resources



## Appendix 1 – high level comments

### **1. Understanding of the time-scale and the future of the project.**

It is important to understand the OT project life cycle. Mongolia has one of the very few known large, relatively rich copper deposits in the world. Sustainably extracting economical value from this natural wealth requires an extremely long development period. Over the eight years of committed work since the Investment Agreement 2009 (IA) signing, revenues from the open pit operation have been used to fund the underground development, which contains the future value of OT. No dividends have been paid to date to any shareholders. Presently, we anticipate sustainable underground production to begin in 2021 after which OT will operate for several years before it recovers its investment and generates taxable profits.

In this context, we are concerned that the report creates a misleading impression that the project already generates great value for the benefit of investors. This is simply not the case as the project is presently being heavily



invested. Although neither the investors nor GoM are receiving dividends, and won't for some time, GoM is receiving and will continue to receive significant tax and royalty income. Following several years of discussion about value sharing between the parties, Rio Tinto, Turquoise Hill, OT and the GoM jointly, with the signing of the 2015 Oyu Tolgoi Underground Mine Development and Financing Plan ("UDP"), reconfirmed the validity of prior agreements and confirmed estimates, based on facts and assumptions current at the time, that approximately 53% of the economic benefit of the project, measured in total undiscounted cash flow, will ultimately belong to GoM. Those fact and assumptions remain valid.

Further, GoM's cash flow from OT has been positive and steady, with no requirement to fund any up front capital for the project's development. Conversely, the investors have provided heavy upfront investment and Rio Tinto has assumed significant risk through its guarantee of the project finance. The investors are not expected to fully recover their funding of development capital provided to OT for several years, by which time the tax contributed by OT will have increased substantially.

## 2. Understanding economic and tax performance to date

As explained above, while it will take time to generate profits, it is important to understand that substantial taxes and royalties have already been paid.

Despite its early stage of development, OT has paid since 2010 approximately \$1.7bn (\$1,641m per the table below plus \$120m paid year to date through Q3 2017 per Turquoise Hill's December 2017 Investor Report<sup>6</sup>) in the form of taxes and royalties, and is already the largest tax payer in the country. These amounts do not include employee income taxes.

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<sup>6</sup> <http://www.turquoisehill.com/i/pdf/ppt/Presentation-Dec-06-2017.pdf>



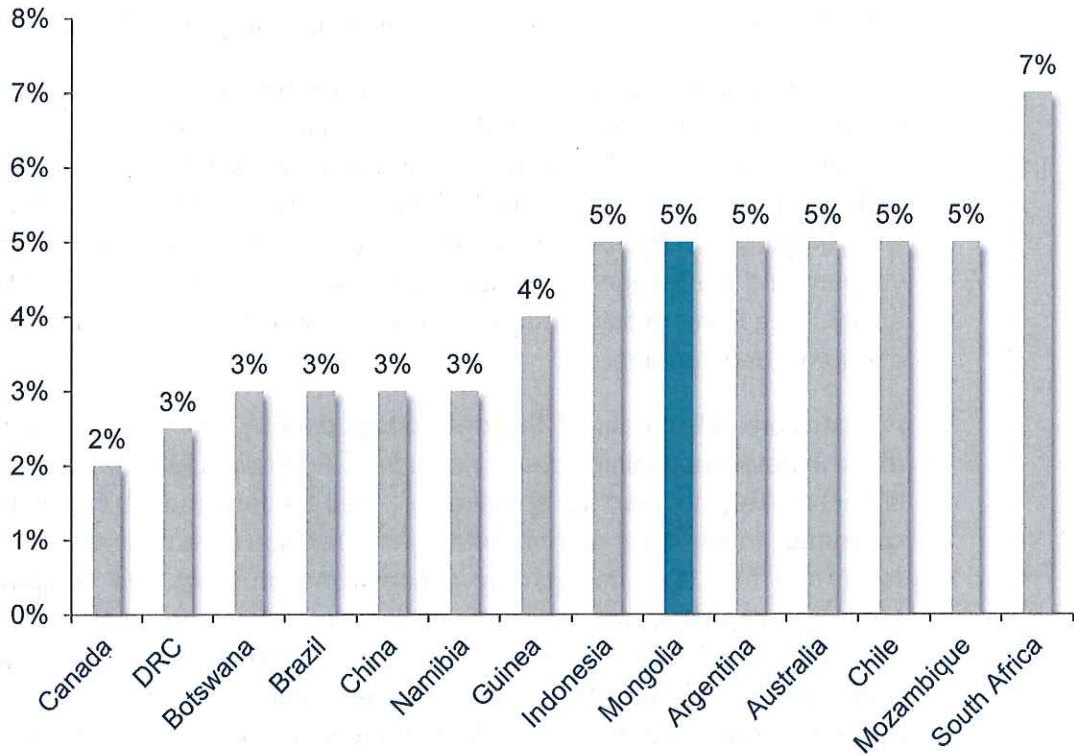
#### Cash Tax Paid from 2010 to 2016

	2010 to 2016 US\$M
Royalty	200
Value Added Tax and Customs	1,003
Corporate Income Tax	No taxable profit
Social Security Tax	87
Withholding Tax	149
Other	202
Total	1,641

Given the capital costs of mine development the project is not expected to commence paying corporate income tax in the medium-term. While the project develops though, the GoM is being compensated for the usage of its mineral resources through royalty payments. These payments occur regardless of whether the company is profitable as long as mining operations continue. The royalty rate that is in effect in Mongolia is comparable to other copper producing countries.



### Effective copper royalty rates in select countries



The mining industry is often welcomed for direct investment by developing countries because experience has shown it can be a significant contributor to the national economic development of a country. In the case of Mongolia, by mid-2020, approximately \$12bln will have been invested in the open-pit and the underground project. From the viewpoint of a global mining company, which has many competing investment alternatives, the decision to invest in a multi-billion dollar project involves an assessment of numerous factors,

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including a comprehensive financial determination of the value of the after tax cash flows from the project. Bearing in mind that a large scale mining project usually has a 50+ year life, there are numerous uncertainties that impact the value calculation. Taxation is one variable in that value calculation.

The mining company objective is to limit the number of variables, such as taxation risk, so that the value calculation can be relied upon when making the investment decisions. Stabilisation of the taxation regime at that time is a key factor in de-risking the tax variable associated with large scale investments in a developing country. Our discussions regarding stabilisation do not occur in a vacuum and we recognise the importance of governments safeguarding their ability to evolve policy and regulation around social, environmental and economic development.

Furthermore, alignment of the developing country tax rules and rates with those in developed mining countries such as Australia, USA, Canada and Chile is more likely to lead to sustainable, well understood and benchmarked outcomes. In particular, appropriate rules in relation to refunds of indirect taxes (VAT and fuel tax), import duty concessions on plant and equipment, an adequate capital allowance write-off regime, low or no withholding tax on dividends and interest, appropriate loss carry forward rules (given that first production is usually 8+ years after the feasibility stage of the project), appropriate debt/equity rules and an independent dispute resolution process are all important “incentives” that merely align the developing country tax system with what is available in developed mining countries. In this regard, the following table illustrates that the stabilised tax regime for OT is aligned in most aspects and certainly not concessionary when compared to Australia, USA, Canada or Chile.





**Comparison of OT Stabilised Tax Attributes to Other Tax Regimes**

	Corporate Tax Rate %	VAT refunded	Typical dividend withholding tax	Typical interest withholding tax	Tax loss carry forward	Typical Debt:Equity ratio
<b>Stabilised OT</b>	25	No	0%	10%	8 years	3:1
<b>Australia</b>	30	Yes	0%	10%	Unlimited	1.5:1
<b>United States</b>	21	Yes	0%	0%	Unlimited	1.5:1
<b>Chile</b>	35	Yes	0%	4%	Unlimited	3:1
<b>Canada</b>	25 to 30	Yes	5%	10%	20 years	1.5:1

We also believe it is important to note OT's greater economic contribution. For example:

- OT is significantly contributing to Mongolia's growth, transacting with 642 domestic suppliers<sup>7</sup> and partners and spending approximately US\$1 billion from January through end of September 2017 with national suppliers for both operational and developmental activities.
- OT is already the largest private sector employer in the country. There are over 13,000 employees and contractors working on the project today.
- OT has withheld and paid over \$88m of employee income tax for 2010 to 2016.<sup>8</sup>
- OT has provided significant mining and technical capability that is being purposefully transferred to the national workforce, designed to help build and operate many other modern and sustainable mines in Mongolia in the future.

<sup>7</sup> <http://ot.mn/scorecard/>

<sup>8</sup> [http://www.riotinto.com/documents/RT\\_taxes\\_paid\\_in\\_2016.pdf](http://www.riotinto.com/documents/RT_taxes_paid_in_2016.pdf)



Furthermore, a successful OT project will demonstrate to international investors that Mongolia is a suitable country in which to invest capital and a country that encourages foreign direct investment. A successful project will create a standard for the Mongolian Government to benchmark future large scale mining projects.

### 3. Safety, Social and Environmental Performance

Safety is OT's core value. OT is one of the safest mines in the world with an AIFR rate of 0.25 (all injury rate for every 200,000 hours of work exposure) through Q3 2017, despite the massive and complex development work currently taking place.<sup>9</sup>

In relation to communities and social performance, we are concerned that the information in the report is not up to date. We also believe it would benefit from reference to a more diverse range of sources. OT has consulted widely with stakeholders since 2002 when exploration activities commenced, and maintains frequent dialogue with local communities and stakeholders. A Partnership Committee has been established to ensure that consultation is ongoing, and that community feedback informs OT's work on social, economic, and environmental issues. Extensive baseline studies and assessments have been conducted with regular and ongoing input from communities, including an Environmental and Social Impact Assessment<sup>10</sup> that follows the Performance Standards of the International Finance Corporation, the global benchmark for such assessments. These efforts have resulted in the development of environmental and social mitigations designed to reduce

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<sup>9</sup> <http://ot.mn/oyu-tolgoi-releases-q3-2017-results-setting-three-operational-records/>

<sup>10</sup> <http://ot.mn/environmental-social-impact-assessment/>



impacts, including eight social and environmental management plans, which are currently being implemented<sup>11</sup>.

Protecting water resources and biodiversity have been issues of central importance. OT has worked closely with stakeholders to address questions and concerns that they have had about the diversion of the Undai River, which has been successful in its aim to protect precious subsurface water in an ephemeral riverbed in the project area. The results have confirmed that there have been no negative impacts to the river system. OT maintains a participatory environmental monitoring program, which involves local communities and herders. This program also confirms no negative impact to water from the project. One spring that was affected by the project has been replaced by a new spring, which was created in consultation with herders. Additional detail about environmental management can be found in OT's closure plan, which discusses a wide range of social and environmental issues, including the issue of subsidence and how the subsidence zone will be managed in a way that is stable and safe.<sup>[2]</sup>

Under a Cooperation Agreement with local communities, OT makes an annual contribution of US\$5 million to the Gobi Oyu Development Support Fund (DSF), an independent fund that supports sustainable community development. Through December 2017, the DSF has invested US\$11 million in 65 projects and programs, which have resulted in the creation of more than 200 permanent jobs, and scholarships for 57 students, among other achievements.

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<sup>11</sup> Please see <http://ot.mn/operation-management-plans/> for these plans.

<sup>[2]</sup> The closure plan is publicly available

at [http://ot.mn/media/ot/content/page\\_content/commitments/ESIA/](http://ot.mn/media/ot/content/page_content/commitments/ESIA/)

[2 Operation Management Plans/13 Mine Closure Plan/ESIA OT OMP Mine Closure Plan EN.pdf](http://ot.mn/media/ot/content/page_content/commitments/ESIA/2%20Operation%20Management%20Plans/13%20Mine%20Closure%20Plan/ESIA%20OMP%20Mine%20Closure%20Plan%20EN.pdf)



OT strives to minimize impacts, or mitigate any residual impacts, and has worked closely with herder households on relocation, compensation, and livelihood support, with independent external monitoring conducted on these processes. OT is pleased with the resolution of the complaint brought to the Office of the Compliance Advisor/Ombudsman (CAO).<sup>[3]</sup> A Tri-partite Council was set up with the herders, local government, and OT, to jointly track and manage actions to resolve any issues related to impacts on herders.

Independent audits assess OT's environmental and social management systems and performance against international standards three times per year, and the audit reports are publicly disclosed.<sup>[4]</sup> In addition, the GoM has an extensive compliance and assurance process, which requires environmental audits to be conducted by provincial and national regulatory agencies each year, addressing issues such as water management. Any actions found as part of these processes are addressed and used to improve OT's social and environmental performance.

#### **4. Taxation Aspects of the OT Fiscal Structure**

Sections 3, 4 and 5 of the report address various aspects of the fiscal structure of OT. We are deeply concerned by the allegation that the current fiscal structure is abusive and would like to provide further context to respond to this view.

##### **There is no reduction of Mongolian Tax**

Like most businesses, OT obtains funding through a mix of debt and equity financing. The appropriate amount of debt leverage a company should obtain is a commercial decision and is not driven by tax motives. Further, in many

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<sup>[3]</sup> The Office has published detail on the case: [http://www.cao-ombudsman.org/cases/case\\_detail.aspx?id=191](http://www.cao-ombudsman.org/cases/case_detail.aspx?id=191)

<sup>[4]</sup> <http://ot.mn/esia-audit-reports/>



countries, including Mongolia, the debt-equity funding ratio is limited. The amount of debt and equity funding provided by the investors is in accordance with the funding structure agreed among OT's shareholders, including both Turquoise Hill and GoM, and the level of OT debt has remained within the ratio legally permitted. Turquoise Hill's debt investment in OT represents additional financial risk; therefore, it is reasonable that the debt should be repaid with interest in due course.

Interest on loans is deductible for Mongolian income tax purposes when paid. When payments are made, the legal residence of the beneficiary of the interest does not impact the deductibility of interest in Mongolia. Therefore, the intermediate funding structure has not resulted in any reduction of Mongolia tax relative to the position that would apply if the structure did not exist.

The legal structure by which the investors provide debt funding to the project also has not resulted in a reduction of Mongolian taxes relative to direct loans from Canada. The rate of Mongolian interest withholding tax under Mongolia's tax treaty with Canada is the same as the agreed-upon rates as stabilised in the IA tying to the stabilised Netherlands and Luxembourg treaties.

**The fiscal structure for OT has been transparently agreed with the Government of Mongolia**

The key agreements are the IA, the Amended and Restated Shareholders Agreement 2011 (ARSHA), and the Underground Mine Development and Funding Plan 2015 (UDP). These agreements are critical in underpinning the investment required to deliver OT and the long term value to Mongolians noted above. The IA sets out a tax regime for the project which is in line with Mongolian law. Given the scale of the required investment, the long period before the investors receive a positive return and the lack of precedent for similar investments in the Mongolian mining sector, the parties agreed that the



tax regime for the project would not adversely change during the term of the IA. Such stabilization is specifically provided for in the Mongolian Minerals Law.

At the time of concluding the UDP a number of key tax principles included in the IA were reconfirmed with the Mongolian Tax Authority under the auspices of the Government. These include the principle of tax stability, including the rates of withholding tax included in the double tax agreements in force at the time of concluding the IA. These confirmations were a fundamental aspect of concluding the UDP which allowed the underground investment to proceed.

In line with international norms, up to 75% of project funding may be provided in the form of debt. The terms of the debt funding were agreed in the ARSHA and the UDP.

It was also agreed that to the extent the Government did not elect to fund their 34% share of equity funding this would be provided by the investors on the same terms as other debt in the structure via non-recourse loans. Repayment of such loans is only required from the Government's future share of project dividends. The Government therefore has no funding at risk whilst capturing this upside value, noting that most host country governments do not require equity participation in mining projects.

The ARSHA contemplates equity funding being provided by Oyu Tolgoi Netherlands BV which is a party to the agreement. It therefore follows that the parties have agreed that the stabilised Dutch treaty would apply to dividends flowing to Oyu Tolgoi Netherlands BV.

### **The Fiscal Structure should be considered as a whole**

We would note in particular that the taxes paid to date include \$1bn of value added tax (VAT) and customs duties. In nearly all host countries domestic VAT is fully refundable to a mining operation that exports its production. The



Investors' acceptance of a fiscal regime under which VAT is not refundable is materially different to international norms.

Many host countries exempt mining projects from customs duties in recognition that the duties only arise as the domestic market does not have the capacity to supply the required goods. No such exemptions apply to OT. The royalty rate on copper production in Mongolia is near the upper end of the global range as demonstrated in the above on page 4, Effective copper royalty rates in select countries.

As demonstrated in the chart on page 5, Comparison of OT Stabilised Tax Attributes to Other Tax Regimes, shows that overall the stabilised tax regime for OT is not out of line with international norms and in some important respects will deliver significantly more value to GoM than comparator regimes.

#### **Substance in Oyu Tolgoi Netherlands BV and Movele Sarl**

The report alleges that there is a lack of substance in Oyu Tolgoi Netherlands BV and Movele Sarl. As these entities operate as intermediate financing companies within the fiscal structure agreed with GoM set out in the project agreements, they do not require a significant number of employees to manage their affairs.

The boards of each company consist of directors with the necessary experience and expertise in mining, commercial and financial issues to effectively manage their affairs. A majority of the board members are resident where the respective companies are resident and the boards regularly meet locally to exercise control and management of the companies.

#### **Legacy Equity Participation via THR Oyu Tolgoi Ltd**

The report notes that a very small proportion (0.21%) of the equity issued by Oyu Tolgoi LLC is held via THR Oyu Tolgoi Ltd which is incorporated in the



BVI and suggests that this is for the avoidance of Mongolian taxes. This is a legacy of the funding structure in place before the project agreements were concluded and no funding has been provided via this company subsequent to 2009. Noting that Mongolia does not have a tax treaty with the BVI this legacy structure does not result in the reduction of any Mongolian taxes.

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## Appendix: suggested factual corrections and added context

Reference	SOMO text	Comment
1.1 (p. 3) The importance of Oyu Tolgoi for Mongolia	“The case of Oyu Tolgoi with its remarkable Investment Agreement, providing Rio Tinto with a favourable tax position protected from legislative changes, raises a number of questions.”	In the light of our wider comments we believe the tax position is fair rather than favourable.
2.2 (p. 9) Oyu Tolgoi’s Corporate Structure	Oyu Tolgoi Corporate Structure Chart	THR Mines (BC) Ltd. owns only 20% of the Co-op. THR Ltd. owns 80% of the Co-op directly. This is not a significant error but is noted for completeness.
2.2 (p. 7) Oyu Tolgoi’s Corporate Structure	“Oyu Tolgoi LLC owns 66% of the Oyu Tolgoi mine, while state-owned company Erdenes Oyu Tolgoi owns the remaining 34%”.	Strictly OT LLC owns the entire mine. The OT LLC equity is held 66% by the investors and 34% by the government via Erdenes a state owned company.
2.3 (p. 10) Finance	“... the Shareholders' Agreement describes that any dividend payments by Oyu Tolgoi LLC to Erdenes Oyu Tolgoi will go to Turquoise Hill Resources until the loans are fully repaid...dividends that GoM will receive from Oyu Tolgoi are minimal...It is therefore likely that the GoM has not received any dividends from the Oyu Tolgoi mine yet.”	As noted above, the direction of GoM’s share of project dividends to repay the Lending Certificate balance is as agreed between the parties as the mechanism available to GoM to fund its equity participation. Failure to explain this creates a misleading impression of GoM being deprived of dividends rights in a way that has not been agreed by the parties. To say “...dividends that GoM will receive from Oyu Tolgoi are minimal...” is speculative and unsupported by actual financial data as noted above. It is unbalanced to state that GoM has not yet received any dividends from the Oyu Tolgoi mine. The project is in its



		development stage and no investors have received any dividends.
3.1 (p. 12) Stabilising Taxes or relinquishing sovereignty?	“The disastrous impact this has had on Mongolia’s tax revenue from the Oyu Tolgoi mine will be explored further in chapter 4.”	As noted above it was transparently agreed with GoM from the inception of the investment in 2009 that treaty rates of withholding tax would apply to the project and that these were explicitly within the stabilised tax regime of the project. This principle, including the rates noted in the SOMO report, was reconfirmed as part of concluding the UDP in 2015. As discussed above no dividends have been paid to any investors to date and are not anticipated for a significant period. In terms of total fiscal revenues from the project dividend withholding tax represents a small proportion. The use of the term “disastrous” is unbalanced in this context.
3.1	These findings put earlier statements by Robert Friedland into a clearer perspective	We note these reported comments were dated 2005 prior to Rio Tinto’s entry to the project and the negotiation of the project agreements. Placing a nuanced interpretation as to their meaning is speculative. The comments may have been referring to the Canada Mongolia double tax agreement.
3.2 (p. 13) Revenue disputes	“Moreover, when the Great Khural audited OT in 2013, it found numerous issues of cost overruns connected with excessive management service fees.”	The thrust of the criticism in this section is that a fair share of project value does not accrue to GoM. See the reference in footnote 62 “...delivers to Turquoise Hill the entirety of OT’s Value”. This criticism does not align with the value split noted above which sees the majority of project value accrue to GoM.
3.2 (p. 13) Revenue disputes	“Furthermore, Rio Tinto gave up a smelter royalty	This language incorrectly implies that OT intentionally withheld royalties that were



	and agreed to pay 10 months' worth of royalties it still owed the GoM."	due. The government accepted the royalty adjustment was due to a genuine difference of interpretation of the basis of calculating royalties in an area where Mongolian tax law and the IA were unclear. The issue was resolved as part of the UDP agreement.
3.2 (p. 13) Revenue disputes	"Rio Tinto and Turquoise Hill Resources agreed to pay an additional \$30 million (instead of the demanded \$300 million) tax claim."	The initial tax assessment was \$130m. After a rigorous dispute resolution process including taking a number of cases through the Mongolian courts the final tax agreed was \$31m. In a project of the scale and complexity of OT it is not unusual to find tax assessments of this amount due to genuine disagreement as to the interpretation of tax law. We also observe that the referenced <i>Sydney Morning Herald</i> article gave the total value of adjustments in GoM's favour as \$148m. GoM confirmed at the time that the dispute was fairly and transparently resolved, as evidenced by the signing of the UDP.
3.3 (p. 13 – 14) The Investment Agreement and Possible Corruption	All of section 3.3	This section irresponsibly and unquestionably repeats speculative assertions that have been firmly denied by Mr Bayartsogt. Insofar as allegations are made against Rio Tinto or Turquoise Hill, they are entirely untrue and there is no evidence to support them. The publication of section 3.3 is likely to cause serious harm to the reputation of Rio Tinto and Turquoise Hill Resources, it is defamatory. We also note that by publishing section 3.3, SOMO would breach its own Code of Conduct for research, including paragraph 3 ("Reliability"). Please confirm



		immediately that section 3.3 will be deleted from any further versions of the report.
4 (p. 15) Tax Avoidance and minimisation	"The Oyu Tolgoi mine's development is financed through loans taken out by the Canadian owner of the mine, Turquoise Hill Resources Ltd."	Other than temporary loans pending equity refinancing Turquoise Hill Resources is not debt funded. This is an important point to keep in mind when reviewing the funding structure for OT (no funding costs are claimed in Canada by Turquoise Hill Resources).
As above	"After receiving the loans, a large part of the capital was moved by Turquoise Hill Resources Ltd. to a subsidiary in Luxembourg, called Movele S.A.R.L."	Movele does not hold the money borrowed by OT to finance the mine. Rather, Rio Tinto temporarily holds the surplus cash and returns the cash to Turquoise Hill to finance the project as required.
As above	"...allows Turquoise Hill and its corporate group to avoid taxes in both Mongolia and Canada."	The funding structure for the project is in line with what was transparently agreed with the GoM in the project agreements. As noted above the funding structure does not reduce Mongolian taxes relative to the position of the funding being provided directly by Turquoise Hill Resources Ltd. It is incorrect to state that any reduction in Mongolian tax has arisen as a result of the structure.
As above	First paragraph, table, and second paragraph	For information Movele no longer makes direct loans to OT LLC and all previous direct loans have been repaid. Furthermore, the balance for loans from Movele to OT LLC was zero in 2016.
4.1 (p. 15) Loans from Luxembourg	"The lack of employees indicates that these two Turquoise Hill Resources subsidiaries function as mailbox companies that exist on paper but	This and similar comments are incorrect. The substance of Movele and Oyu Tolgoi Netherlands BV is addressed in the body of the response above Under Substance in Oyu Tolgoi Netherlands BV and Movele Sarl.



	undertake little real economic activity."	
As above (p. 16)	"The nearly US\$800 million in interest expenses for Oyu Tolgoi LLC has led to a matching decrease in the company's taxable profit, which has likely decreased the company's taxable base and tax revenue for the Mongolian state."	The financing structure for the project, including the proportion of debt funding and the terms on which debt funding is advanced are in line with the project agreements concluded with GoM. The quantum of interest expense is therefore as per the agreed position with GoM. Tax relief for such expense is achieved in full compliance with Mongolian tax laws. Interest is only deductible for Mongolian purposes when paid. To date \$149m of Mongolian withholding tax on interest has been paid notwithstanding that no effective relief has been obtained for interest expense as Oyu Tolgoi is in a tax loss position.
As above (p. 17)	"OT Netherlands BV is registered as a cooperative, which allows TRQ to avoid Dutch withholding taxes on dividend. It is still unclear to what extent the OT Netherlands may be used to avoid future tax on capital gains."	OTNBV is not a cooperative but rather is owned by a cooperative. The tax treatment of the Netherlands entities has been agreed with the Dutch tax authorities and is aligned with local practice. No Dutch withholding tax or Mongolian capital gains tax has arisen as a consequence of the structure and no such avoidance is anticipated to arise in future.
4.2 (p. 17) Tax deal in Luxembourg – avoiding Canadian taxes	Title – Avoiding Canadian Taxes	The funding structure is in compliance with Canadian tax laws and is broadly available to all taxpayers and has been confirmed with the Canadian Revenue Authority via tax rulings.
As above	Table 4	We would note that the referenced interest income is not required to be recognised for Canadian tax purposes under Canadian tax rules. To recognise



		such income would generate a non-required material Canadian tax cost for the group on accrued interest income at a time when there are no Canadian interest costs. This Canadian cost would reduce the funding available for investment in Mongolia.
4.3 Oyu Tolgoi's abusive Investment Agreement – minimalizing Mongolian tax obligations	Title – “Abusive investment agreement”	<p>This section proceeds from the assumption that the application of reduced rates of withholding tax via double taxation agreements (“DTA’s”) between countries is “Abusive” DTA’s are agreements reached between countries to mitigate double-taxation and encourage cross-border investment among nations.</p> <p>The investment agreement (“IA”) stabilised the treaty rates of withholding tax in force at the commencement of the project in a transparent manner and the investment has proceeded on the basis that such treaty rates would be respected. The applicability of the stabilised treaty rates has been subsequently conformed and agreed with the Mongolian tax authorities in particular as part of agreeing the UDP in 2015 which permitted the underground investment to proceed. It is incorrect to describe this aspect of the Investment Agreement as abusive.</p>
As above (p. 21)	“...the company managed to get the government to lower the WHT rate on interest paid by Oyu Tolgoi LLC from 10% to 6.6%.”	Similar to equity funding, GoM has the right to provide debt funding to OT. It was agreed in the shareholders agreement that to the extent the investors provided the government's 34% debt funding obligation then the

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		investors would not be penalised by needing to pay interest withholding tax on what would otherwise have been the government's share. Thus, Turquoise Hill bears the burden of withholding tax only relative to the 66% portion of its equity ownership.
As above (p. 22)	".. it seems that if Oyu Tolgoi paid tax following domestic law instead of the abusive Investment Agreement, the GoM would be able to almost double its annual budget for education	Once again we strongly reject the allegation that the IA is abusive and believe that this statement does not take into account the broader context of the project and associated benefits. It is also worth noting that the relevant tax law as stabilised included items materially in the GoM's favour relative to international norms notably the non-recovery of VAT.
As above (p. 20)	"Luxembourg and Mongolia did not have a DTA."	The treaty was signed in 1998 and was terminated in 2014 post the signing of the Investment Agreement. When the IA was signed in 2009 it was agreed that treaties in force at the commencement of the investment were stabilised.
5. Treaty abuse using Dutch mailbox companies	Title	We have noted that it has been transparent since the commencement of the investment that the equity investor in Oyu Tolgoi LLC would be Oyu Tolgoi Netherlands BV. We have also noted the tax consequences of this have been conformed with the GoM and the Mongolian Tax Authority on several occasions and that these are built into the agreed value apportionment for the project. We have also addressed that the company has sufficient local substance in the Netherlands to conduct its business there. We also confirm that one of the factors in selecting a Netherlands



		based investor was the bilateral investor protection treaty between Netherlands and Mongolia noting no such treaty existed with Canada at the time. We disagree that the utilisation of the bilateral investor protection should be discarded as “illegitimate” where it is legally obtained to protect the project from significant non-tax risks.
As above (p. 23)	“Turquoise Hill subsidiary Movele – arguably the real investor in Oyu Tolgoi – is registered in Luxembourg, a country that does not have a BIT with Mongolia”	Given the detailed analysis of the structure included in the report we do not understand the point made here and do not believe that the comment is supportable.

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