



Position Paper

Fostering a Modern Commodity Exchange Ecosystem in Nigeria

This position paper is developed as part of the mapping and analysis of national legislations, regulations and policies relevant for business enabling environment, trade and competitiveness, MSMEs and value chains development in Nigeria, commissioned by Nigeria Competitiveness Project (NICOP) and implemented in partnership with Centre for Trade and Business Environment Advocacy (CTBA) and Federal Ministry of Industry, Trade and Investment. NICOP is co-funded by the European Union (EU) and the German Government; and implemented by GIZ SEDIN Programme with the Federal Ministry of Industry, Trade and Investment (FMITI) as national partner.

1. Introduction

The regulatory framework for commodities exchange in Nigeria is the Investment and Securities Act (ISA) 2007 and the “Requirements for Registration as Commodities Exchange Operators” issued by the Securities and Exchange Commission (SEC) pursuant to the ISA. The ISA mentions “commodity exchanges” in section 13(b) as one of the entities under the regulatory purview of the SEC. However, apart from the Requirements for “Registration as Commodities Exchange Operators”, there is no definite framework to regulate the operation of commodity exchanges under the Act. In recognition of the need to improve the commodity trading market/ecosystem, SEC set up a Technical Committee on Commodities Trading Ecosystem in 2017 with the mandate “to identify challenges of the existing framework/infrastructure and develop a roadmap for a vibrant ecosystem”. The Reportⁱ of the Committee was exposed stakeholders’ comments in the first quarter of 2018.

With the demise of commodity boards and commodity marketing companies in the mid-1980s, a number of challenges arose in respect of price discovery, produce aggregation and grading, etc. The gap created by the demise of the commodity boards was brought to light with the comments of the immediate past Minister for Agriculture and Rural Development, Chief Audu Ogbe when he announced that he was considering bringing back the commodity boards, thereby sparking off a debate on the subjectⁱⁱ. The two top arguments in favour of the return of the commodity boards revolved around the need to ensure the quality of produce, especially those destined for export markets; and transparency in market/price information. Those against the idea raised issues about the monopolistic powers of commodity boards as well as the bureaucratic inefficiency that may overtake its running. The debate also recognised the alternative approach presented by privately run commodity exchange system in addressing the gap left by the commodity boards.

The commodity exchange system plays an important role in fixing certain marketing frictions that clog the commodities markets. The frictions include low price of commodities at the farm gate due to lack of proper market information and product aggregation services; poor access to credit by commodity producers (especially farmers) due to lack of collateral; lack of proper grading and standardisation leading to rejection of commodities; losses occasioned by poor logistics; etc. Besides formalising commodity trading in Nigeria, an efficient commodity trading ecosystem anchored on commodity exchanges would also deepen the financial market by creating new



tradable instruments in form of contracts and derivatives; generate new investments in agriculture and agro-processing, warehousing, logistics, and other support services that make up the exchange ecosystem.

2. Context

It is important to state that past attempts at establishing a commodity exchange in Nigeria failed primarily because it was government owned and got starved of funding before it could stabiliseⁱⁱⁱ. The idea of setting up the commodity exchange started in 1989 when, in recognition of the vacuum created by the defunct Produce Marketing Boards, the government set up an inter-ministerial committee to consider the possibility of setting up commodity exchanges as an alternative. No action was taking on the recommendation of the committee, which was in favour of setting up commodity exchanges, up until 2001 when the government directed the conversion of the Abuja Stock Exchange to a Commodity Exchange – first called Abuja Commodity Exchange, then Abuja Security and Commodity Exchange (ASCE) and now called the Nigerian Commodity Exchange (NCX). The Exchange did not commence trading until 2006. Besides the issue of funding, the SEC Committee Report identified other factors that contribute to the failure of the Exchange as follows: “weak supply, lack of interest by operators in the securities market to open commodities trading subsidiaries, low understanding of the workings of the Exchange and the absence of supportive infrastructure and institutional arrangements that could strengthen the supply side of the market”. The report also mentioned the absence of organized farmers’ cooperatives for bulking of produce, commodity grades and standards as well as farmers’ credit system based on Warehouse Receipts as contributing factors to the failure of the Exchange. The NCX was recently reported to be undergoing privatization with the Nigerian Sovereign Investment Authority as the main investor.

Today, there is only one operational commodity exchange in Nigeria, the privately owned AFEX Commodities Exchange Limited (AFEX), a sister company of East Africa Exchange (EAX), which was established in Nigeria in 2014^{iv}. AFEX operates a Warehouse Receipt System and maintains warehouses in different locations across even states in Northern and North-Central Nigeria. A second exchange, the Lagos Commodity and Futures Exchange was licensed in 2019 but has not started trading^v.

The SEC Committee report raised pertinent issues that need to be resolved in creating a definite regulatory and operational framework for commodity exchange ecosystem in Nigeria. It recommended far reaching regulatory changes such as the reduction in the minimum paid-up capital of commodity brokers, streamlining regulation to take into account the different segments of the market (spot trading, futures, etc), better definition of regulatory mandate of the various MDAs within the ecosystem (Federal Ministry of Finance, Federal Ministry of Agriculture and Rural Development, Federal Ministry of Industry, Trade and Investment, Standard Organisation of Nigeria, etc); the report also recommended for advocacy and capacity building across the various stakeholders and potential investors to ensure that the concept of commodity exchange is properly understood and embraced. Although the Committee identified most of the relevant stakeholders within the ecosystem, the scope of the Committee’s work did not extend to interviewing the stakeholders. In other words, the report has not captured the current thoughts of all relevant stakeholders from the government and the private sector on the way forward for the establishment of a functional commodity trading ecosystem in Nigeria.



On the regulatory framework, it is important to point out that there are currently at least three Bills before the National Assembly that seek to regulate different aspects of the commodity trading ecosystem^{vi}. Of note is the Commodities Exchanges Commission Bill which seeks to create a new regulator, with accompanying substantive rules for commodity exchanges. Other Bills seek to regulate independent warehousing, commodity brokering, etc.

3. Commodity Market Reform Bills

From the foregoing analysis, it is evident that the commodity market in Nigeria is not properly organised. This means that farmers are not able to get the right value for their produce. Also, they are denied the opportunity to access financing using their commodities as security. As a result of the interest and effort of various stakeholders to address this over time, several Bills have been prepared and presented to the National Assembly over the year but none of them have become law till date. These Bills have resurfaced in the 9th National Assembly and require the concerted effort of stakeholders to scale through to becoming laws. They include the Commodities Exchange Commission Bill, the Nigerian Independent Warehouse Regulatory Agency (Establishment Bill), and Warehouse Receipt Bill.

a. *Commodities Exchange Bill, 2019*

This is a Bill for an Act to “regulate commodities future trading in Nigeria; provide for the establishment of the Commodities Future Trading Commission and for related matters”. The Bill lays out a regulatory framework for “Commodity Exchanges and Trading Facilities and Derivates Exchanges in Nigeria”. The Commission proposed under the Bill would have the power to register and regulate exchanges and participants/operators in the commodities and futures markets, including prescribing the eligibility for licencing as an exchange and the different participants in the market (Sections 8, 20, and 29). Section 20 details the powers of the Commission with respect to the registration of Commodity Exchange or Derivative Trading Facility. These bodies are supposed to be self-regulating – having their own rules which must satisfy the provision of the law before they can be registered. The Commission also has the powers to revoke the operating license of a Commodity Exchange or Derivative Trading Facility (Section 22) as well as superintend over the disciplinary processes undertaken by the Commodity Exchanges or Derivate Trading Facilities over an operator within those markets.

Section 29 details the powers of the Commission with respect to the registration of “commodity market operators”, which include “floor dealer, floor broker, sub-broker, transfer agent, future commission merchant, commodity pool operator, commodity trading adviser and such other intermediaries associated with the commodities industry”. The commission also retains the power to cancel or suspend any license granted to a commodity market operator. The Bill contains sundry rules aimed at safeguarding the integrity of commodity transactions within the Exchanges. There are rules against margin trading and market rigging transactions (Section 38); commodities market manipulation (Section 39); false or misleading statements (Section 40); fraudulently inducing person to deal in security (Section 41); dissemination of illegal information (Section 42); prohibition of fraudulent means (Section 43); prohibition of insider dealings (Section 45); etc. The Bill further proposes appropriate penalties and remedies for contravention.

Appeals lie from the decisions or actions of the Commission to the Securities and Exchange Tribunal set up under the Investment and Securities Act (ISA) of 2007 (Section 59). The Bill further



seeks to save the provisions of the ISA that relate to commodity trading but further proposes that the provisions of the Bill take precedence where there is inconsistency between it and the ISA, or any other law (Section 70).

b. Nigeria Independent Warehouse Regulatory Agency (Establishment) Bill

The warehouse receipt system allows the owner or producer of a commodity to deposit the commodity in a licensed warehouse in exchange for a receipt which serves as a proof of the depositor's proprietary interest over (as well as the quality and quantity of) the commodity, and which can be used as security for loan or transferred to a third part. The only system that comes close to this is the private warehouse receipt system operated by AFEX.

This Bill seeks to “establish the Nigeria Independent Warehouse Regulatory Agency to regulate the operations of licensed warehouses and to provide a regulatory framework for trading in warehouse receipts and for related matters”. Section 1 of the Bill lists the Objectives as follows: establish the Nigeria Independent Warehouse Regulatory Agency; provide regulatory framework for trading in warehouse receipts; institutionalise best practices in commercial warehousing in Nigeria; enable depositors store and retrieve agricultural and other commodities in commercial warehouses; and enhance the issuance and use of negotiable warehouse receipts as valid negotiable instruments and acceptable collateral by financial institutions in Nigeria.

The Agency proposed under the Bill would have the power to license and regulate warehouse operations, including the various operators, inspectors, samplers, graders, and weightiers (sic); the Agency also has the responsibility to establish and maintain links between the Warehouse Receipt Registry and the existing commodity exchanges (Section 9). Warehouse receipts are tradable in commodity exchanges (Section 40). Section 67 prohibits the operation of a commercial warehouse without a license issued by the Agency. Section 68 gives the Agency the power to create a transitional window of not more than two years for existing commercial warehouse operators to fully comply and bring their operations in line with the provisions of the Act. There are also provision relating to conditions for issuance, suspension, and revocation of licenses.

The Bill proposes a Central Registry for Warehouse Receipts, to be run by the Agency, where all warehouse receipts issued under the Bill (Act) would be registered – including any cancellation, modification or endorsement thereon (sections 81 and 83). The Registrar (DG) would maintain the Register, while provisions would be made for online operations of the Central Registry (Section 84). Other rules contained in the Bill relate to safeguarding the integrity of the system, including penalties for contravention of the rules.

c. The Warehouse Receipt Bill

This Bill is another version of the Nigeria Independent Warehouse Regulatory Agency (NIWRA) Bill. The provisions are the same in substance, but the Warehouse Receipt (WR) Bill is a better draft in terms of clarity of language as well as contains some additional provisions. For example, in enumerating the functions of the proposed Agency, the Warehouse Receipt Bill has additional functions such as: classify licensed warehouses into categories; provide requisite training for licensed certified warehouse operators and persons employed in the licensed warehouses; promote awareness and use of Warehouse Receipts; create electronic linkage between the Warehouse receipts registry and existing commodity exchanges. Other functions relate to the



application of weights and measures and quality standards to the commodities under the scheme. The Agency is also mandated, in consultation with the Minister, to develop a programme to support the setting up of processing centres and increased capacity for the processing of stored agricultural products by licensed Warehouse Operators (Section 7 subsection (1)). Also compare the provisions of Section 9(2) of the NIWRA Bill and Section 7(2) of the present Bill as it relates to the investigative and enforcement powers of the Agency. An additional provision in the present Bill allows the Agency to take steps to ensure the attendance of witnesses and production of records and information in carrying out investigation into Warehouse operations.

However, one problematic provision common to the two Bills is found in Section 9(1)(d) of the NIWRA Bill and Section 7(1)(d) of the WR Bill. In the former Bill, it states one of the functions of the Agency as “certify licenced warehouse operators...”; while in the latter Bill, it says “certify in licence warehouse operators...”. It is obvious that there is something missing in the wording of these provisions. In the first mentioned Bill, there is a question as to whose responsibility it is to license the operators that would be certified by the Agency. The provision in the second mentioned Bill which reads “certify in license warehouse operators...” makes no grammatical sense. This provision found in both Bills captures a cardinal function of the Agency, hence the need to ensure clarity in the expression. It is suggested that the paragraph should read “certify and license warehouse operators...”. The implication is that the Agency would have the power to run certification programmes/examinations as a pre-condition to licensing.

Further on the comparison between the two Bills, the arrangement of the Parts and Sections are different in the two Bills, but it seems that the arrangement of the WR Bill is preferable.

4. Recommendations on commodity market reforms

It has been noted above that the function of commodity exchange regulation is being performed by the SEC under the ISA. Some questions to be considered by the government and the stakeholders in designing a regulatory framework for commodity exchange include: Does Nigeria need a separate regulator for commodity exchanges, or should SEC be strengthened to effectively perform that role? Should the government still own commodity exchanges? How many commodity exchanges – private and public – can Nigeria maintain? Some of the options for reforming the commodity market include:

- i. Establish one new regulator: Establish a new regulatory body for commodity exchange in Nigeria. This would mean enacting the Commodities and Exchange Commission Bill, and expressly repealing the powers of SEC in this regard. In following this option, it is necessary to merge (at least incorporate elements of) the Warehouse Receipt Bill, while leaving out the Agency proposed under the Bill. This would leave the proposed Commodities Exchange and Futures Trading Commission to also manage the warehouse receipt system. This approach would be in line with the policy of government to streamline merge existing agencies and avoid creating new ones as much as possible. Ethiopia has a dedicated commodity exchange law and regulator but also a warehouse receipt system lawⁱⁱⁱ, which was initially placed under the mandate of the Ministry of Trade but when the Ethiopia Commodity Exchange was set up in 2008, it was assigned the responsibility for managing the warehouse receipt system. In essence, the warehouse receipt system is an integral part of the Ethiopian Commodity Exchange ecosystem.



- ii. Pass a new legislation to regulate warehouse receipt system, but do not establish a new regulator for warehouse receipts: this approach would (a) retain the powers of SEC in respect of Commodity Exchanges but enact the Warehouse Receipts Bill to enable the utilisation of the warehouse receipt system within the commodity exchange ecosystem in Nigeria. This approach would also involve the strengthening of the capacity of the SEC to license and regulate commodity exchange operations. To achieve this, SEC would need to issue a comprehensive regulation on commodity exchange operations. In the alternative, the ISA could be amended with the aim of spelling out more clearly the powers of SEC in respect of the commodity exchange operation. Here also the experience of Ethiopia is instructive. Different laws and regulators existed for commodity exchange and warehouse receipt. The regulator of the warehouse receipt system in Ethiopia is the Ministry of Trade (which has now assigned the responsibility to the Ethiopian Commodity Exchange) while the Ethiopia Commodity Exchange Authority (ECEA) regulates the Commodity Exchange itself. However, we recommend that Nigeria avoids setting up a regulator just for the warehouse receipt system but may consider assigning this function to a dedicated unit in the Federal Ministry of Industry Trade and Investment.
- iii. No new regulator and no new legislation: the approach would involve the following: (a) retain the regulatory powers of SEC in respect of commodity exchanges, then solve the problem of lack of details of the powers of SEC as enshrined in the ISA by issuing new regulations (by SEC) to close the gap in the ISA. (b) include warehouse receipt system as part of the new commodity exchange regulation. There are experiences from across Africa to show that the operations of the warehouse receipt system are usually tied to the commodity exchange ecosystem^{viii}. In fact, in Ghana, the securities regulator regulates the commodity exchange and warehouse receipts system^{ix}. The Ghana Security and Exchange Commission issued Guidelines on Commodity Exchange^x and Warehouse Receipts^{xi} in 2019.

There is a need to pursue process of dialogue that could lead to the resolution of these issues and the adoption of a common approach. The adopted approach would then form the basis for the development of a comprehensive regulatory framework for commodity exchange and warehouse receipt system in Nigeria.

ⁱ <https://sec.gov.ng/exposure-of-the-report-of-the-technical-committee-on-enhancing-the-commodities-trading-ecosystem/>

ⁱⁱ <https://www.pressreader.com/nigeria/business-a-m/20180903/281805694805289>

ⁱⁱⁱ Ibid

^{iv} <https://afexnigeria.com/>

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[https://www.lcfe.ng/about.html#:~:text=Lagos%20Commodities%20and%20Futures%20Exchange%20\(LCFE\)%20was%20incorporated%20in%20May.trading%20of%204%20Asset%20classes.](https://www.lcfe.ng/about.html#:~:text=Lagos%20Commodities%20and%20Futures%20Exchange%20(LCFE)%20was%20incorporated%20in%20May.trading%20of%204%20Asset%20classes.)



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- vi These Bills are analysed in Section 5 of the Report
- vii <http://extwprlegs1.fao.org/docs/pdf/eth145717.pdf>
- viii <https://pdfs.semanticscholar.org/fa8f/c05ae5cafbea996280e357de06074782f46b.pdf>
- ix <http://moti.gov.gh/docs/GCX%20Project.pdf>
- x http://sec.gov.gh/wp-content/uploads/Final-Regulatory-Laws/Guidelines/Commodity_Exchange_Guidelines_2019.pdf
- xi http://sec.gov.gh/wp-content/uploads/Final-Regulatory-Laws/Guidelines/WAREHOUSE_RECEIPTS_2019.pdf