



PROSPECTS OF COMMODITY TRADE DEVELOPMENT IN SES



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Contents

List of Abbreviations	7
Summary of the Report	9
1. The evolution of commodity exchange principles	12
2. The effect of commodity exchange on state development and trends in exchange market trading	18
3. Commodity exchange trading: international experience	24
3.1. Current trends in the development of organised commodity trade	27
4. The main phases of development of the commodity exchanges in Russia and Kazakhstan	34
4.1. Russia	34
4.2. Kazakhstan	38
5. Cooperation between the SES countries on organised commodity markets	44
5.1. Member state legislation regulating organised commodity markets, market participants and standard exchange contracts and exchange commodity regulations and restrictions	45
5.2. Analysis of member state legislation relating to electronic document distribution and the use of electronic digital signatures in cross-border transactions	60
5.3. National systems for regulating clearing and activities involving transactions with basic commodity market assets	62
5.4. National settlement and currency regulation systems for international transactions involving basic commodity exchange assets	63
5.5. Existing conditions supporting integration of an organised commodities market	63
6. Main conclusions	66
References	67

Tables

Table 1.	Chronology of the evolution of the commodity exchange	14
Table 2.	Elements of commodity exchange regulation	20
Table 3.	Commodity futures and options market dynamics	25
Table 4.	Global futures and options volume by region	26
Table 5.	The top ten Derivatives Exchanges ranked by number of contracts traded and/or cleared	26
Table 6.	Important mergers and takeovers of commodity exchanges	28–29
Table 7.	Volume of commodity futures by selected commodity exchanges	31
Table 8.	Main phases of commodity exchange development in Russia	35–36
Table 9.	Main events in the development of commodity exchange trading in Kazakhstan	39–40
Table 10.	Comparative data on the commodity exchanges of Kazakhstan, Russia and Ukraine	42

Figures

Figure 1.	Evolution of the commodity exchange as an organisation	13
Figure 2.	The commodity market at different stages of economic development	18
Figure 3.	Regulation of the futures market in the USA	22
Figure 4.	Distribution of transactions by category	24
Figure 5.	Commodity futures and options market dynamics	25
Figure 6.	Volume of contracts traded and/or cleared in January–July 2012	26
Figure 7.	Global futures and options volume by region	32
Figure 8.	Number of exchanges and commodity floors on the commodity and stock markets	37
Figure 9.	Primary activities on Russian commodity markets	37

Figure 10.	Commodity exchange turnover from transactions involving real goods (not including futures transactions)	38
Figure 11.	Exchange turnover by type of operation	38
Figure 12.	Number of commodity exchanges in Kazakhstan	41
Figure 13.	Volume of exchange trading	41
Figure 14.	Exchange turnover from transactions	41
Figure 15.	Exchange turnover by type of operation	43

List of Abbreviations

BCE – Brazilian Commodity Exchange
BM&F – Brazilian Mercantile & Futures Exchange
BMSP – Bolsa de Mercadorias de Sao Paulo
BBF – Bolsa Brasileira de Futuros
BUCE – Belarus Universal Commodity Exchange
CBOT – Chicago Board of Trade
CFTC – Commodity Futures Trading Commission
CIS – Commonwealth of Independent States
CME – Chicago Mercantile Exchange
COMMEMEX – Commodity and Monetary Exchange of Malaysia
CFTC – Commodity Futures Trading Commission
CU – Customs Union
CSCE – Coffee, Sugar & Cocoa Exchange Inc.
DTB – Deutsche Termin Boerse
EDB – Eurasian Development Bank
EurAsEC – Eurasian Economic Community
ETS – Eurasian Trading System
FAS – Federal Antimonopoly Service
FTZ – Free Trade Zone
FSSS – Federal State Statistics Service
FCM – Futures Commission Merchants
FIA – Futures Industry Association
IAE CIS – International Association of Exchanges of the CIS countries
ICE – IntercontinentalExchange

LCE – London Commodity Exchange

MICEX – Moscow Interbank Currency Exchange

NASDAQ – National Association of Securities Dealers Automated Quote

NFA – National Futures Association

NYMEX – New York Mercantile Exchange

NYCE – New York Cotton Exchange

NYBOT – New York Board of Trade

NYSE – New York Stock Exchange

PJSC – Private Joint Stock Company

RTS – Russian Trading System

SEC – US Securities and Exchange Commission

SES – Single Economic Space

SOFFEX – Swiss Options and Financial Futures Exchange

UNCTAD – United Nations Conference for Trading and Development

VAT – value added tax

Summary of the Report

Commodity exchanges account for nearly 20% of operations involving trade in raw materials. This fact predetermines the role international commodity markets play in establishing and regulating world prices. Quotations on the London Metal Exchange determine the prices for trade in metals worldwide. Exchange quotations serve as price indicators for nearly all of the global trade in grain, cocoa beans, cotton, rubber and many other commodities. In addition, commodity exchanges act as a source of market information, including price information, for off-exchange trading. Exchange operations are actively used to hedge against commodity price volatility. The commodity exchange is not only a place for concluding transactions, but also an information centre concerning any particular traded commodity.

Nowadays, some 60–70 different commodities are traded on commodity exchanges. The production and trading of every commodity are subject to specific international regulation. This regulation is intended to balance production and international trade in raw materials. It is used to coordinate production, consumption and marketing policies and thereby smooth out sudden price fluctuations on the global markets.

Commodity exchanges have evolved from local markets trading physical commodities to high-liquidity international markets trading futures and forward contracts. They are an excellent example of a self-regulating market institute and have become an integral part of the production and financial operations of a vast number of economic entities. Whilst maintaining their original characteristics – ensuring transparency of the trading process and competitiveness in the concluding of transactions – commodity exchanges have improved technically and in terms of the number of different operations performed and contracts handled.

Development of the commodity exchange market is a spur to improving market infrastructure, credit relations and the banking system, the system of insuring against commercial risk, the clearing and settlement system, the legal environment, and so on. These assertions are supported by research carried out by United Nations Conference on Trade and Development (UNCTAD).

UNCTAD published a number of interesting reports and studies during the first ten years of this millennium. In one publication examining the development role of commodity exchanges (UNCTAD, 2007), commodity exchanges are seen as institutions able to facilitate trade and stimulate economic growth in developing countries by reducing transaction costs along the commodity supply chain. This research suggests there is a link between activity on commodity exchanges and improvements in the wider economy. For example, the development of a warehouse network to improve the delivery and collateral management processes can substantially enhance the storage and logistics infrastructure for the traded commodities. A reliable system of collateral management – in particular warehouse receipts – provides greater security and lowers risks for banks to lend to

commodity producers, increasing the attractiveness of commodity finance as a credit instrument.

In many developing countries, according to UNCTAD research, exchange mechanisms promote the wider involvement of isolated commodity sector participants in economic relations. It should be remembered that profits are not generated merely by the establishment of a commodity exchange. The commodity exchange mechanism requires complex regulation. The role of the government within the regulatory structure is twofold. An oversight role is about preventing market manipulation and ensuring contracts are inviolable. An enabling role is about creating the necessary legal and regulatory environment and, where necessary, elements of physical infrastructure.

Regulation has three objectives: to guarantee market integrity, to uphold financial integrity and to protect investors from the malpractice or irresponsible activities of exchanges, counterparties or market intermediaries. Global commodity market experience suggests that the futures market is a highly regulated environment with a multi-layered system of oversight. The oversight these “layers” provide is often mutually reinforcing. Unfortunately, they cannot totally eradicate malpractice, examples of which periodically make the headlines.

Commodity exchanges operate in both open and restricted economies. Some were created on a wave of economic reforms, others during political transformation and the transition to free market economy. There are commodity exchanges in countries where small-scale domestic production predominates, and also in countries whose economic systems combine large-scale commercial production and small-scale producers. In some countries, commodity exchanges serve domestic markets, in others they are aimed at exports. While many commodity exchanges operate in countries where market infrastructures, institutions and procedures are highly developed, and national markets are well integrated, they have also been successfully established in countries whose markets are in need of further development and integration. Commodity exchange trading is continually developing and trading operations are becoming ever more complex. Notable trends in the sector include: a reduction in the number of commodity exchanges; the merging of specialised commodity markets into universal commodity exchanges; changes in the role and function of the commodity exchange as a financial institution; technological developments and growth in the number of commodity exchange participants; the gradual unification of commodity exchange organisations on a global scale; and changes in the way commodity exchange operations are regulated.

The revival of activity on the Russian commodity exchange was a milestone in the country’s transition to a market economy. Initially, as the command system of supply collapsed, commodity exchanges facilitated the trade in commodities. Commodity exchanges were a focal point around which investment, insurance and brokering companies, trading houses and commercial banks were founded. They also attracted capital, which was then reinvested in profitable companies and in improving IT infrastructure. Among the most important achievements of commodity exchanges has been their contribution to nurturing the first cadre of home-grown business professionals.

Despite its turbulent history, the Russian exchange sector is following international development trends thanks to its adoption of international standards and best practices

in the operations of Russian exchanges and market regulators and the proximity of highly competitive foreign markets.

Exchange trading in Kazakhstan has still not matched the status and turnover it enjoys in the West and in Russia. The country's commodity exchange sector is still in development. However, for Kazakhstan, as the exporting country with huge raw material and agrarian capacity, the proliferation of exchange trade is seen as viable. With the creation in 2008 of the Eurasian Trading System (ETS) and adoption of the Law on Commodity Exchange in 2009, Kazakhstan has entered a new phase in commodity trade development.

Although there are similarities between the commodity exchanges as they were developing in Russia and Kazakhstan, the differences between them are nevertheless more remarkable. One notable similarity is that both experienced a slowing down of market activity as a result of state interference. In Russia, the regulation of commodity exchanges was tightened up in 1992 coinciding with an increase in taxation and price liberalisation. In Kazakhstan, permanent revision of legislation governing commodity exchange trading has hindered the setting of a level playing field. In both countries, the state has maintained zealous oversight of stock markets in the absence of a comprehensive support programme. Another similarity between the countries is the failure to establish the same level of infrastructure and regulation for commodity exchanges as exists for the stock market.

The final part of this report presents the results of research undertaken jointly by the Eurasian Development Bank (EDB) and the International Association of Exchanges of the CIS (IAE CIS) on commodity market regulation in Russia, Kazakhstan, Belarus and Ukraine. Research has shown that regulation of commodity exchanges in Russia, Kazakhstan and Belarus is hindering interexchange cooperation on organised commodity markets. It is now time, research suggests, to define and adopt priorities for the development of an organised interstate commodity exchange. This will require a more detailed analysis of the problems that affect such cooperation; it also calls for the development of a long-term strategy to create a competitive interstate commodity market. It is clear that the differences in legislation regulating organised commodity markets and trading activity are a serious stumbling block to interexchange cooperation. As already mentioned, the regulation of organised commodity markets lags far behind that of the stock markets or the banking sector. Legislation needs to be drafted which takes into account fully the specific characteristics of an organised commodities market.

It has been suggested that the results of comparative analysis of the regulation of organised commodities market in CIS countries be used to develop a comprehensive commodity exchange model for CIS member states and the SES, based on common principles of operation, provision of access to professional participants, regulation of trading floor procedures and size of assets, information transparency, contract guarantees and risk management.

A large number of issues will need to be addressed in order to achieve the necessary level of legislative unification between the member states. This will require collaboration between regulators, commodity exchanges, industry association (IAE CIS) and other interested parties. A special oversight authority dedicated to the sector should be created to coordinate development efforts in the organised commodity market, similar to those established for the stock markets in the CIS and EurAsEC regional organisations.

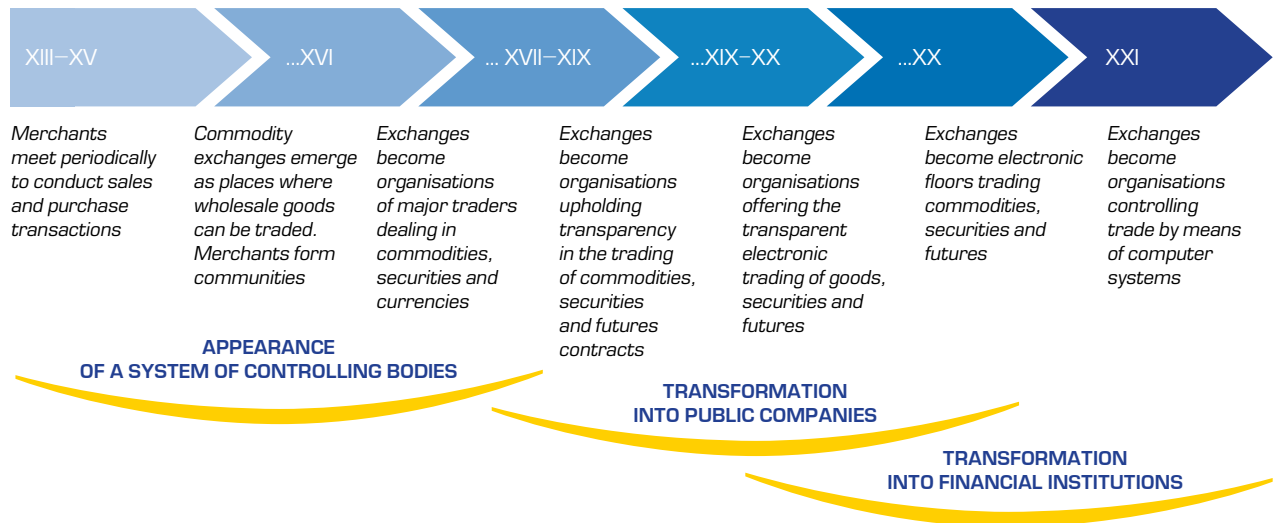
1. The Evolution of Commodity Exchange Principles

- **Modern commodity exchanges are the product of the lengthy evolution of different forms of wholesale trading and is one of the types of an organised commodity market**
- **As a market mechanism, the commodity exchange has several stabilising functions in the wider economy**
- **The commodity exchange acts chiefly as a “focal point” for trading operations whilst also increasing transaction security**

In Ozhegov’s explanatory dictionary of the Russian language,, a “commodity exchange” is defined as “an institution, in which financial and commercial transactions are carried out with securities, currency or bulk commodities, bought and sold in accordance with reference norms and standards”. This definition could in fact be applied to almost all the development phases the commodity exchange has passed through up to now. The commodity exchange is not just an institution or establishment, however; it is also an organised market. In order to understand the commodity exchange fully, we must be aware of its history.

Today’s commodity exchange and its principles – based initially upon the trading of goods – is the product of many centuries of evolution. The fundamental principles of the commodity exchange can still be seen to operate in street markets, stalls, bazaars and fairs. The idea of exchanging goods existed even before the first human settlements appeared. It was the Sumerians who first thought up the idea of money in the fourth millennium BCE. They used tokens made of clay to “represent” a commodity. Later on, this figurative representation evolved into simple marks carved onto clay – the first known writing system. The development of market economics in the late Middle Ages and the abandonment of subsistence farming and direct consumption led to an increase in the turnover of goods and trading thus became more sophisticated. Long before the appearance of the first stock exchanges, “forward trading” was introduced as an effective way of moving agricultural products from producer to consumer at previously agreed prices and under established delivery conditions. There is evidence that the forward trading of rice was practised in China some 6,000 years ago. In Japan, in the 17th century, contracts for the supply of rice – so-called “rice tickets” – served as a form of currency and could be traded commercially.

This abbreviated history shows that commodity exchanges were not the invention of a single nation or group of people. It also demonstrates how free markets turned into organised



markets, how exchange-traded commodity appeared, how market of physical goods transformed into a market of the entitlement to goods and how functions of organising sales turned into functions of servicing trade.

Even in the early stages of commodity market development, economists and historians (e.g., Schtillick, 1912; Dimitriev, 1863; Filippov, 1912) were attempting to assign specific characteristics to and establish the commodity exchange as both a market and an institution. These authors used a range of criteria, bringing into common parlance terms such as “transparency and competitiveness”, “organisational availability”, “the interchangeability of goods quoted (but not present on) the commodity exchange”, “uniformity of price in respect of goods of a given type and quality” and “the existence of officially-established exchange rates and quotes”.

It is notable that the majority of these terms retain their meaning on the commodity market as we understand it today. These days, trading on the commodity market is to all intents and purposes – “virtual”. The vast majority of transactions do not result in the supply of the goods purchased, but rather in the payment of differences in price. Commodity exchange transactions are carried out on the basis of standard commodity exchange contracts, in accordance with which the period of delivery of the goods and their quality is strictly regulated. The goods traded are not actually present on the commodity exchange; indeed, they are not intended to be physically present and they are not subject to any kind of prior inspection. Purchasers on the commodity exchange are not actually buying any identifiable good or commodity, but rather a document confirming their entitlement to ownership of that good, normally in the form of an options or futures contract. Thanks to this method of organising trade, the volume of goods on the commodity exchanges has increased one hundred-fold from the time when trading consisted of the buying and selling of physical goods.

Among the existing descriptions and definitions of commodity exchanges, the version offered by Filippov in 1912 is particularly interesting. It reads: “The commodity exchange is a special type of market, historically taking the form of regular meetings held in an

Figure 1.

Evolution of the commodity exchange as an organisation

1. THE EVOLUTION OF COMMODITY EXCHANGE PRINCIPLES

8 th –15 th centuries	16 th –18 th centuries	19 th –20 th centuries
<p>Special markets and fairs for the exchange of goods. Distinctive features – regular trade, confinement of trade to a specific place and a set of predetermined regulations. As specialisation developed, some fairs focused on trade between English, Flemish, Spanish, French and Italian merchants.</p> <p>The most common type of transaction was that of an “on-the-spot” cash settlement with immediate delivery of the goods; however, the practice had already begun of concluding contracts for delivery of goods of an agreed quality within a specified time.</p>	<p>Market trading had already become more organised, including through the provision of designated market places and established trading practices, forms of credit to facilitate trading, a legal system covering transactions and the provision of brokering and information services. Town and city authorities were given the power to settle disputes. A gradual shift towards trading in “sample goods” led to the establishment of quality standards. Market places gradually turned into centres of international trade.</p>	<p>The Industrial Revolution at the end of the 18th and beginning of the 19th centuries led to a marked rise in market trading. Giant leaps in productivity in all industries took trade to a new level, giving rise to commodity exchanges as we understand them today.</p> <p>Futures trading (wholesale, remote, non-cash transactions) emerged; this type of trading focused on standard contracts, identical in terms of the quantity and quality of the goods, delivery and other conditions. All contract standards are set by the exchange, with pricing and quantity the only variables. Exchanges start to act as guarantors for implementation of the terms specified in trading contracts.</p>
<p>Among the most important contributions the medieval fair made to modern commercial activities were its principles of self-regulation and arbitration and the formalisation of trading processes.</p> <p>In medieval England, laws governing the merchant activities determined the standards required by local authorities. These formed the basis of generally accepted practices covering the registration of transactions, trading accounts, receipts of carriage and storage, letters of credit, acts of transfer and other documents. Those breaking the rules could be expelled from the merchant community and banned from trading.</p> <p>The principle of self-regulation is founded in English common law. According to this principle, associations of merchants had the right to enforce their own rules of conduct and this led to the establishment of wholesale traders’ courts. In the 14th century, these courts were formally adopted as courts of common law. In England, their jurisdiction was subordinate to that of local courts.</p>	<p>The first European markets – in the modern sense – began to appear in the 16th century. In Bruges, where the term “exchange” was first used, merchants concluded transactions using bills, rather than real commodities. The term “exchange” referred specifically to meetings of Italian merchants, although the merchants of other nationalities also held identical trading sessions. This fragmentation of trade was a feature of medieval markets. The merchants of each nationality had their own special privileges, which prevented them uniting into a single corporation. This fragmentation was ended in Antwerp.</p> <p>In 1531, exchange meetings moved from Bruges to Antwerp, where the exchange market became even more sophisticated. It was in Antwerp that the first international exchange appeared – the prototype of the modern commodity exchange.</p> <p>In the 17th and 18th centuries the Amsterdam Commodity Exchange (1608) became Europe’s leading centre for trade. For the first time, trading was conducted on the basis of samples. Average quality standards for goods were established, shares were put into circulation and speculation began. Simultaneously with the Amsterdam Commodity Exchange, exchanges sprang up in London and Paris and later in Frankfurt-am-Main, Hamburg, Berlin and Vienna.</p> <p>The first specialised exchanges trading exclusively in grain appeared in Amsterdam in the 17th century.</p>	<p>The most industrialised country at the beginning of the 19th century was Great Britain. The trading centre for British goods during the Industrial Revolution was the Royal Exchange. Trading had begun on this site in 1561.</p> <p>At the beginning of the 19th century, the list of commodities included cereals, tea, wool and spices, complemented by coal, cotton, metals and ores. No commodity exchange standards yet existed; trading was conducted on the basis of samples. Over time, the volume of trade increased, the number of commodity traders increased and separate trading groups emerged based on commodity type.</p> <p>In the US, futures in the modern sense appeared in Chicago in the middle of the 19th century. With the opening in 1848 of the Illinois-Michigan Canal, Chicago became a transit point for trade between the agricultural producers of the Midwest and consumers in the densely populated commercial and industrial towns of the east coast. In 1848, the first Chicago commodity exchange, the Board of Trade of the City of Chicago, was set up by a group of 82 local traders. The exchange allowed the trading of a wide range of commodities to be concentrated in one place.</p> <p>In London and Chicago, the volume of trade increased with brokers working on the same type of commodities. This led to the adoption of agreed standard contracts.</p> <p>By 1865, the Chicago exchange was exclusively trading futures based on the supply of agricultural commodities.</p> <p>Commodity exchanges appeared in New York between 1870 and 1880. These exchanges normally specialised in just a small number of commodities, such as coffee, cotton, sugar or cocoa beans. In 1872, trading in dairy products began with the opening of the New York Cheese and Butter Exchange. Later, trading in eggs, poultry, preserves and dried fruits began on the same site. In 1882, the exchange changed its name to the New York Commodity Exchange. Eggs and butter were also traded at a specialised exchange in Chicago, opened in 1898. Twenty years later, the exchange was renamed the Chicago Commodity Exchange. By the start of the 21st century, this exchange had developed into one of the world’s largest derivatives trading sites.</p>

Table 1.
Chronology of the evolution of the commodity exchange

established place and with fixed organisation. It is a market on which trade is carried out under special transaction regulations, concentrating on the bulk purchase of interchangeable goods at prices regulated under inherent terms of reference.” Filippov identified four basic types of commodity exchange and differentiated them according to the levels of state intervention in commodity exchange transactions and the type of market organisation – open or restricted.

A more modern version of the term “commodity exchange”, and the one currently used by experts at UNCTAD dealing with issues of trade and commodity exchange development, reads: “Commodity exchanges are understood as any organised market, on which trading operations are centralised.” In this definition, no obligatory physical presence of the goods is implied – only the concluding of transactions. It is important that all transactions are carried out in accordance with a unified mechanism – one providing effective competition between all the vendors and between all the purchasers. This definition also includes auctions, but does not include wholesale markets, in which trading – whilst localised in character – is represented by a multitude of unconnected, individual transactions concluded between different types of vendors and purchasers” (UNCTAD, 1997).

The commodity exchange is, therefore, seen as a special, historically formed economic institution, the character of which reflects the legal and economic transformation of internal, informal markets into organised exchanges.

As a market mechanism, the commodity exchange carries out a range of stabilising functions in the wider economy. These functions include trading services in the wider sense, the provision of liquidity and the optimal distribution of essential raw materials, and the stabilisation of prices and costs, currency exchange, money supply and loans.

The commodity exchanges can specialise in the trading of options and futures contracts – as practised by almost all commodity exchanges in the west – or they can operate primarily as centres for transactions involving physical commodities. In both cases, the main attribute of the commodity exchange is its ability to act as a “focal point” for trading operations and to increase transaction security.

There are two types of commodity exchange organisation. The first type includes those exchanges which have a public legal character (widespread among the countries of continental Europe), monitored by the state and created on the basis of commodity exchange legislation. These commodity exchanges allow any entrepreneur to participate, provided he/she is registered and can demonstrate the required levels of turnover established by the given commodity exchange. The second type – those having a private legal character – is made up of the British and American grain, cotton, rubber and non-ferrous metals exchanges – i.e., the main part of the commodity exchange. Access to these exchanges is only granted to a restricted circle of participants belonging to the commodity exchange corporation.

Commodity exchanges themselves are also categorised according to purpose (specialised and general) and by type of operation (physical goods and futures markets).

The evolution of commodity exchanges and market trading is also reflected in the type of goods traded, i.e., the exchange commodities. Just as trading according to sample of commodity was being introduced on the commodity exchange, demands for large-scale

production, uniformity and divisibility began to emerge. With time, essential attributes such as of fixed quality (standards) were introduced. Of course, these attributes were of greater importance to agricultural products and raw materials, which in fact represent the majority of goods sold on the commodity exchange.

On today's commodity markets, around 20% of operations involve raw materials (Velyaminov, 2004) and approximately 70 different types of commodity are traded, including metals (rare, non-noble and precious); the so-called "soft goods" (such as sugar, tea, coffee, cocoa); fuels (oil and gas); and seeds, grain and even domestic cattle.

Two-thirds of the commodities sold on international commodity exchanges are goods produced by the agricultural and forestry industries (mainly oil seed and its derivatives, grain, live animals and meat). Fuels (crude oil and its derivatives) account more than half of the total turnover of the industrial raw materials and derivatives group. Precious metals (gold, silver, platinum and palladium) account for 30% of the turnover in this group – non-ferrous metals (copper, tin, brass, zinc, nickel and aluminium) account for 20%.



The production and sale of every commodity are controlled by specific international regulations. The aim of regulation is to balance production and normalise international trade in raw materials. Regulation is enacted through the coordination of production policy, consumption, marketing and the stabilising of dramatic fluctuations in global prices.

Following the establishment of United Nations Conference on Trade and Development in 1964, functions of coordination of international cooperation in the global markets in raw material commodities concentrated in the Raw Materials Committee of UNCTAD. The UNCTAD platform was used to develop trade agreements, plans and parameters for different forms of cooperation. In 1976, a programme of integration for raw materials commodities was adopted with the aim of reorganising international trade in such goods based on multiparty trade agreements and trade organisations. In 1980, an intergovernmental agreement on the creation of a mutual stock of raw material commodities was developed with the intention of stabilising global prices.

At the start of the third millennium, the majority of raw materials and products are now bought and sold through the medium of so-called “off-exchange trading”. On the commodity exchanges, the most important commodities are traded as futures and options. This way of organising trade has allowed the volume of commodities traded to increase some one hundred-fold since the period when real goods were traded on the commodity exchange. This trend does, however, carry a degree of risk for the market. This will be looked at in more detail in the sections on prospects for the commodity exchange and commodity market development.

2. The Effect of Commodity Exchange on State Development and Trends in Exchange Market Trading

- **Commodity markets are an integral part of a smooth-running economy**
- **Commodity markets are able to stimulate growth in relevant sectors of the economies of developing countries**
- **Innovative application of commodity market mechanisms leads to the wider involvement in economic relations of previously isolated goods sector participants**

The role of the commodity market at different stages of economic development can be illustrated as follows (see Figure 2).

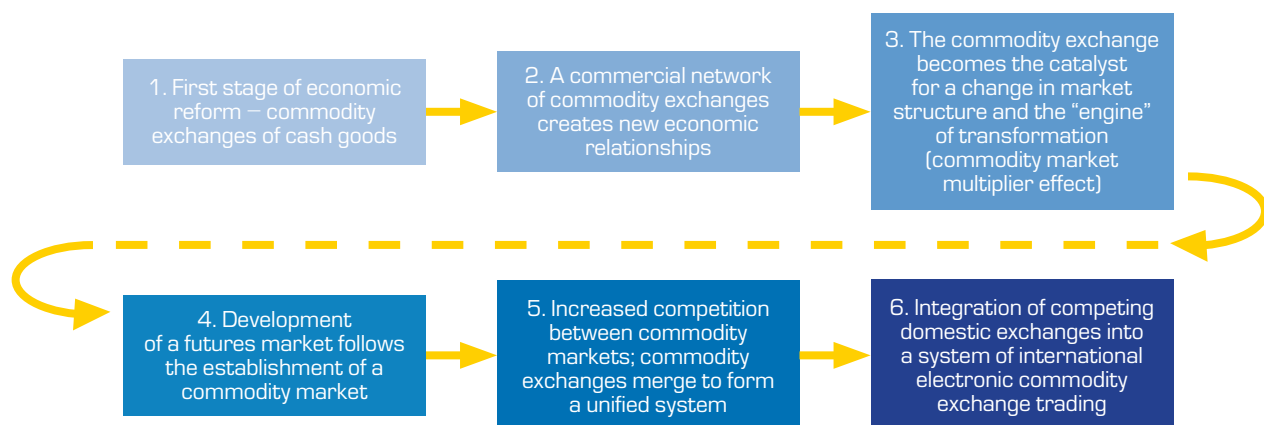


Figure 2. The entire history of the commodities exchange market bears witness to the role it plays in economic relations, first and foremost as the link between buyers and sellers. Its development “stimulates” formation of the institutional infrastructures of a market, including exchange infrastructure, credit relations and the banking system, insurance of commercial risk, the clearing and settlement system, the legal basis for new commercial relations and so on. The effect of the commodity exchange on the system of economic relations is

demonstrated, for example, by the reduction of transportation and associated costs. By introducing specific standards for the commodities marketed, cost reductions relating to the quality of the goods supplied are achieved. The commodity market serves as a centre for the collection and processing of commercial information on the pricing of various types of commodity. The concentration of trade in one place allows equilibrium prices to be established relatively quickly and ensures that these reflect current market conditions. In addition, commodity market trading regulations promote transparency and help the market mechanism to function smoothly.

Specialised international organisations, including UN agencies, have made long-term studies of the issues related to the development of trade and the effects of trade on state development. One of the leading agencies in this field is the UNCTAD. During the first decade of this millennium, this agency published a wealth of research. In one publication dedicated to the role of the commodity exchange in the development of the state (UNCTAD, 2007) commodity exchanges are seen as institutions for trade cooperation, able to stimulate growth in the trading sectors of the economies of developing countries by reducing transaction costs in commodity supply chains. The research suggests that there is a link between commodity market activity and an improved environment for the development of related sectors. If, for example, the commodity exchange stimulates development of a network of storage facilities to enhance supply efficiencies and the provision of credit, this can have a positive effect on warehousing conditions and the logistical infrastructure for the goods being traded. The presence of a reliable system of credit – in particular for warehousing receipts – may, in turn, lower the banks' credit risk for agricultural producers and increase the attractiveness of goods financing as a credit instrument.

UNCTAD's research includes a range of interesting material on the experiences of different states. In Latin American countries, for example, "innovative application" of the commodity market mechanism has led to the greater involvement in economic relations of previously isolated participants of the goods sector. Financing is one of three areas upon which commodity exchanges have had a particular impact. On the Colombian and Venezuelan commodity exchanges, for example, mechanisms have been created to allow the commodities sector to bypass the banks and access local capital markets using the sale and repurchase agreements made by farmers on the exchanges. These tools are especially attractive in cases where banks are not willing to lend to farmers because of the potentially high risks involved. The second area is distribution. On the Panamanian and Honduran commodity markets, exchange mechanisms are used to apply tariffs and commodities import quotas on competing goods. Commodity exchange mediation and established market regulations are helping to broaden options for participation and also improve procedural transparency. The third area of innovation is the market development mechanism. In 2002, on the Brazilian BM&F, a specialised agricultural market (the Brazilian Commodity Exchange – BCE) was set up to link the agricultural sector to trade, industry, finance and the government. Having successfully united six isolated regional markets, the BCE's aim was to develop and commercialise the country's agricultural sector and become a reliable and transparent mechanism for implementing state agricultural policy.

As stated above, profits are not generated as a direct result of the creation of commodity exchanges. The commodity exchange mechanism requires complex regulation. The

Table 2.

Elements of commodity exchange regulation

Source: UNCTAD, 2007b

state plays a dual role in this process: as watchdog (eradicating malpractice and market manipulation and enforcing contractual obligations) and enabler (creating the necessary legal and regulatory environment and, where necessary, elements of physical infrastructure).

Regulation has three objectives: to provide cohesion and integrity in the market (market integrity), to provide a financial system (financial integrity) and to protect the interests of investors from malpractice or the irresponsible behaviour of counterparties and market intermediaries. Regulation is effected at three levels – on the market as a whole; on the

Objectives	Market Level	Exchange Level	Intermediaries Level
Market integrity	<ul style="list-style-type: none"> Registration and licensing of exchanges, clearing houses and intermediaries Procedures for approval of new contracts Supervision aimed at preventing manipulation of the market, non-competitive behaviour and other malpractice Auditing of self-regulating organisations (SROs) Information exchange with foreign regulators to monitor participants and/or cross-border transactions Legal framework for the application of sanctions on market participants or institutions in cases of malpractice 	<ul style="list-style-type: none"> Registration of transaction results indicating time and date Transparent reporting of prices and other market information for all participants Toughening up of requirements on position limits Audio and video monitoring of trading floor activity Accreditation and monitoring of warehouse activity Statutory requirements on exchange staff in respect of information security 	<ul style="list-style-type: none"> Statutory requirements on intermediaries in respect of their qualifications and financial standing Requirements on clients in respect of transparency (compliance with anti-money laundering agreements) Protection of clients from malpractice and misuse of funds
Financial system integrity	<ul style="list-style-type: none"> Minimum capital requirements on clearing houses Financial reporting requirements on brokers and intermediaries Requirements for application of statutory accounting standards to open market positions 	<ul style="list-style-type: none"> Minimal capital requirements on clearing members Availability of clearing house guarantee funds to compensate member losses in the event of default (fund created by clearing member contributions and insured against default) Special measures for high volatility cases – suspension of trading, weak periods and special margins 	<ul style="list-style-type: none"> Marginal client deposits Minimal requirements for client capital holdings
Investor protection	<ul style="list-style-type: none"> Legislative base to provide the following: (i) recognition by counterparties of the legal basis of contracts and contract obligations; (ii) definition of legal relationship between parties in the conclusion of transactions, clearing, settlement and delivery (clients, brokers, exchanges, clearing houses and the banks through which payments are made) Monitoring of exchanges to ensure fair and equal services to all clients Supervision of commodity exchange governing bodies, ensuring representation of the interests of all major shareholders at board level 	<ul style="list-style-type: none"> Well-defined, transparent and binding legislation regulating the activities of exchanges and, in particular, delivery Binding mechanisms of arbitration for dispute resolution between members Binding mechanisms for the application of sanction on members defaulting on transaction obligations 	<ul style="list-style-type: none"> Qualification standards, licensing of intermediaries Standards in the field of marketing practices of intermediaries (advertising, client acquisition, disclosure of information on the cost of services) Separation of financial resources of clients and brokers Requirements on brokers to employ "best practice" in their operations

commodity exchange; and on the brokerage between the commodity exchange and the consumer. Generally speaking, global commodity market experience has shown the futures market¹ to be a highly regulated environment with a multilayered system of supervision, in which the various “layers” are mutually reinforcing. *Table 2* shows the standard elements of a regulatory system according to the objectives and level of application of the system.

These are regarded as the basic elements that guarantee the effectiveness of a regulatory system. In practice, governments regulate market participation – to a greater or lesser degree – in order to provide a balance between maximisation of benefits that regulation brings along to market participants against the costs imposed on them in the performance of the regulatory functions. Governments also face a challenge to find a balance between external regulation by a government authority and self-regulation by the industry or its representative bodies. The balance which governments seek to achieve is, therefore, determined by the level of trust the state and the market participants themselves have in the institutions set up to act as self-regulating organisations. A plan of the system of regulation of the US futures market is offered as an example (see Figure 3).

The system appears well thought out and completely reliable. And yet scandals continue to emerge involving representatives of the sector. These result in serious losses for clients and repercussions for the entire sector. For example, the annual report of the National Futures Association (NFA) for 2012 (NFA, 2012) publishes a letter from Daniel J. Roth, its president and executive director, and Christopher K. Hehmeyer, chairman of the board, which reports on the collapse, in 2011, of one of the largest futures commission merchants – MF Global Inc. The shortfall of \$1.6 billion of client credit – which should have been separated from the fund’s financial resources, deposited into segregated client accounts and presented in financial statements – shattered confidence in the futures markets and their financial integrity. In June 2012, a fresh scandal emerged when the Peregrine Financial Group announced insolvency after revealing that the president of the company had used clients’ designated accounts for his own purposes and falsified financial accounts to the NFA. Over a nine-month period, therefore, it was twice demonstrated to clients of futures commission merchants that they could no longer consider their segregated accounts to be safe and secure.

On April 21, 2010, *Vedomosti* reported that the US Securities and Exchange Commission (SEC) had accused the American investment bank Goldman Sachs of concealing information about the bank’s finances, in order intentionally to mislead shareholders. It was reported that Goldman Sachs investors stood to lose up to \$1 billion due to the speculative activities of the bank’s management. The price of the Troy ounce on the New York Stock Exchange (NYSE) fell by 0.7% during April 19 alone. This scandal affected not only the US commodity exchanges, but also many other exchanges worldwide. This came not long after the activities of fraudsters such as Bernard Madoff (2008, losses in the region of \$65 billion), Alan Stanford (2009, losses in the region of \$8 billion), Jerome Kervel (2008, losses in the region of \$8 billion) had made the headlines (see: <http://nyse-trade.ru/>). In 2004, the reputation of the NYSE had suffered in the wake of revelations

¹ At the beginning of the third millennium, raw materials and goods are chiefly traded under off-exchange conditions, whilst futures and options on the main commodities are traded on stock exchanges.

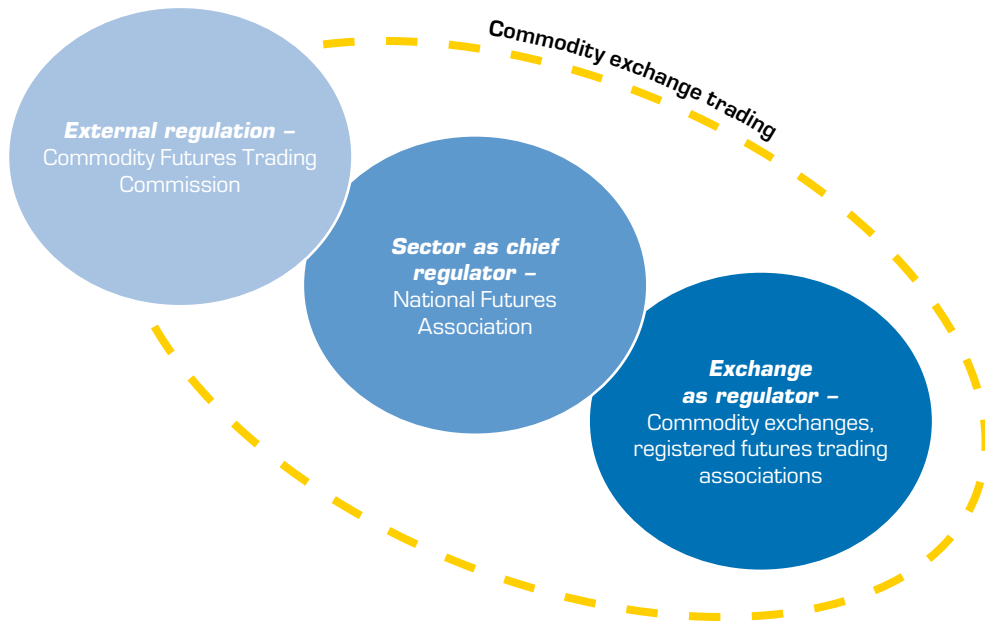


Figure 3.
Regulation
of the futures
market in the USA

INFORMATION:

The CFTC was created by the US Congress in 1974 as an independent government agency. The agency's mandate has been renewed and expanded several times since then. Today, the CFTC is authorised to regulate commodity futures and option markets in the United States and to protect market participants and the public from manipulation and malpractice relating to the trading of commodities, financial futures and options. Apart from the markets and their participants, the CFTC also supervises commodity exchanges, clearing organisations, brokers, dealers, consultants, fund managers and the representatives thereof.

The NFA is a specialised, sector-wide, self-regulating organisation for futures trading. Established in 1982 "to protect the rights of the participants of the futures market by providing ethics in futures and other (including currency) markets and to protect the interests of traders and investors". All broker companies licensed by the organisation are obliged to comply with its requirements and the regulations of the commodity exchanges on which they trade. These are designed to provide financial reliability, rigorous compliance with US federal financial regulations in respect of the procedures used for paying off orders, the submission of reports on stock exchange and Internet trading, the financial limits on positions, the defining of trader price limits, trading policy standards and commercial behaviour. Infringements of stock exchange regulations are subject to financial penalties, suspension or withdrawal of the NFA licence. The organisation unites 3800 companies and 55 thousand associate members. The organisation is financed solely by membership contributions and fees paid by trading participants for futures market appraisals.

Stock exchanges and registered futures associations are obliged to introduce minimum financial and financial reporting standards for all members.

concerning illegal trading and bonuses of \$187.5 billion paid out to Richard Grasso, former chairman of the board of directors. Attention focused on the New York Mercantile Exchange – NYMEX. It turned out that its former head had been involved in commodity exchange manipulation (Kommersant, 1996). So, the question arises as to how this affects countries, in which the infrastructure, institutes, regulatory systems and practices are still in their development stage. In all probability, the very lack of development of those markets offers a measure of self-protection, since a broad spectrum of commodity market instruments is not yet in operation and there is no great difference in standing between the market participants.

What is interesting, however, is that commodity markets function in both open and restricted economies. Some were created on a wave of economic reforms, others during political transformation and the transition to free market economics. There are commodity exchanges in countries whose economic systems combine large-scale commercial production and small-scale producers. In some countries, commodity markets serve domestic markets, in others they are aimed at exports. While many commodity exchanges operate in countries in which the market infrastructure, institutions and procedures are highly developed, and national markets are well integrated, they have also been successfully established in countries whose markets are in need of further development and integration. Commodity exchange trading is continually developing and trading operations are becoming ever more complex. The important trends in the development of the commodity exchange sector will be discussed in the next section.

3. Commodity Exchange Trading: International Experience

- The transition from trading in real goods to trading in their derivatives has changed the basic function of the commodity exchange from an organisation for selling goods to a trading service
- Trading in commodities nowadays has less to do with real economics and is becoming ever more part of the financial market
- Despite the widening geography of commodity exchange trading, the main exchanges are concentrated in the world's leading financial centres

There are around 150 commodity exchanges operating worldwide, trading some 70 different commodities (agricultural and energy raw material, metals and other industrial raw materials). According to international organisations, they account for between 5% and 20% of world trade in exchange commodities. Most of the world's commodity exchanges deal in agricultural produce, but the leading exchanges handle crude oil and oil derivatives, precious metals and non-ferrous metals.

Figure 5 shows the total turnover from futures and options trading by type of commodity (or rather by respective indices) during the first half of 2012, as published by the Futures Industry Magazine in 2013. Futures Industry Association collects data on the number of contracts traded and/or cleared on 84 exchanges worldwide, but not the cost of contracts.

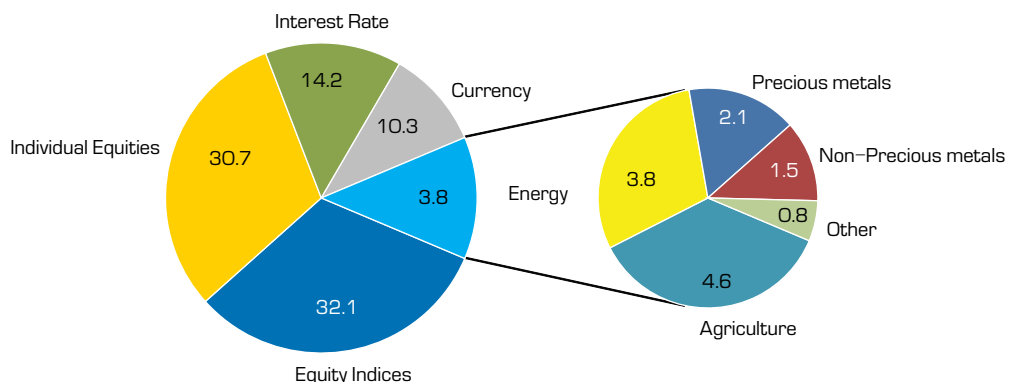


Figure 4.

Distribution of transactions by category (%)

Source: FIM, 2013

The diagram illustrates the general breakdown between financial and commodity futures and options in the total turnover for the first half of 2012. The data for 2012 indicate that agriculture (4.6%) is the largest individual element of commodity futures and options trade. The section labelled “other” (0.8%) includes exotic contracts, based on commodity indices, credits, fertilizers, housing, inflation, plastics and weather. More data on market dynamics is provided in *Figure 6*.

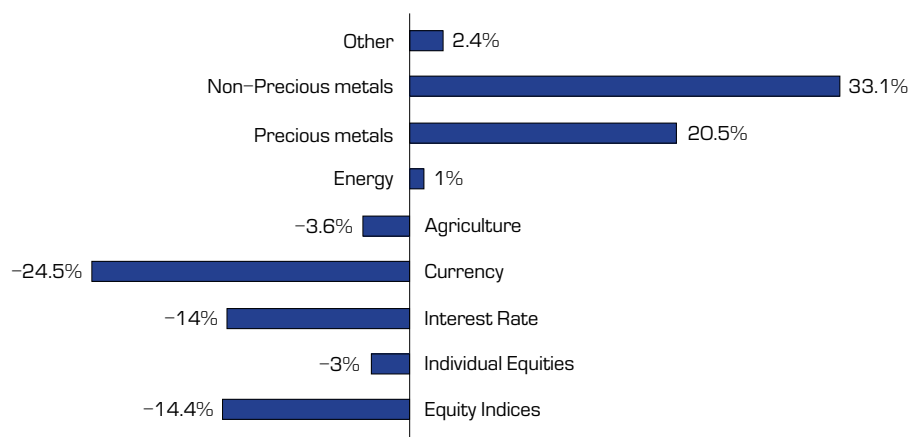


Figure 5.
Commodity futures and options market dynamics (2011–2012)

Source: FIM, 2013

Trading in agricultural futures and options showed negative growth compared to the first half of 2011. Energy trade increased slightly. There was an appreciable growth in trading in futures contracts and options for precious and non-precious metals. The negative dynamics of these indices compared with January–June 2011 – is particularly remarkable.

Type	Dynamic 2010/2011 (%)	Dynamic 2011/2012 (%)
Equity Indices	14	-14.4
Individual Equities	6.1	-3
% rate	11.6	-14
Currency	22	-24.5
Agriculture	-9.1	-3.6
Energy	16	1
Precious metals	-37.7	20.5
Non-precious metals	49.8	33.1
Other	71.3	2.4
Total	10.2	-10.2

Table 3.
Commodity futures and options market dynamics (2010–2012)

Source: FIM, 2013

In the breakdown of global futures and options volume by region, Latin American growth (+19.3%) stands out, although commodity exchange turnover in the Latin American countries is considerably lower than in other regions (see Table 4).

In 2011 all regions demonstrated positive growth compared to the same period in 2010. The Asia–Pacific region grew by 16.4%, North America by 10.3%, Europe by 3% and Latin America by 0.7%.

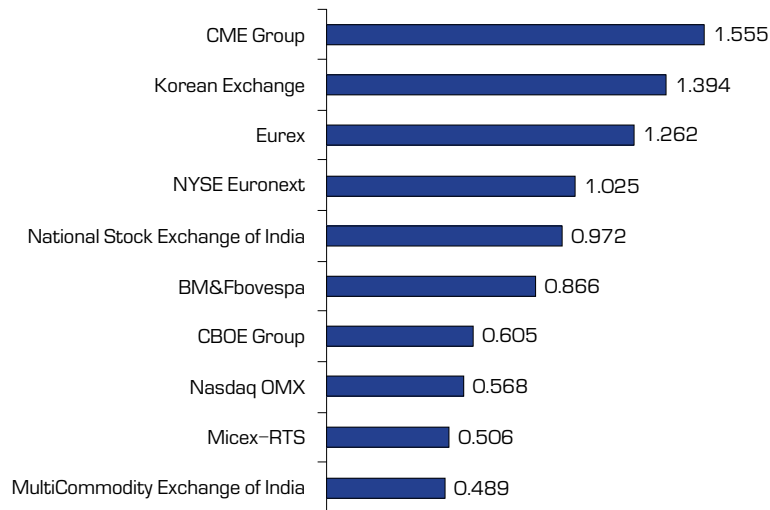
Table 4.
Global futures and options volume by region (\$ billion)
Source: FIM, 2013

Region	January-June 2011	January-June 2012	Dynamic (%)
Asia Pacific	4.91	3.96	-19.3
North America	4.04	3.76	-7
Europe	2.5	2.32	-7
Latin America	0.78	0.93	19.4
Other	0.17	0.16	-7.1
Totals	12.4	11.13	-10.2

Table 5.
The top ten Derivatives Exchanges ranked by number of contracts traded and/or cleared (2011-2012)
Source: FIM, 2013

Rank 2012	Annual % Change 2011-2012	Commodity Exchange	Annual % Change 2010-2011	Rank 2011
1	-8.9	CME Group	8.7	2
2	-34.4	Korean Exchange	19.2	1
3	-11.1	Eurex	-4.4	3
4	-12.2	NYSE Euronext	-3.4	4
5	-7.2	National Commodity Exchange of India	33.7	5
6	19.1	BM&Fbovespa	0.8	6
7	1.7	CBOE Group	-2.8	8
8	-13	Nasdaq OMX	28.5	7
9	10.6	Micex-RTS	58.1	10
10	-13.8	MultiCommodity Exchange of India	2.2	9

Figure 6.
Volume of contracts traded and/or cleared in January-July 2012
Source: FIM, 2013



To complete this brief statistical overview, the data and dynamics of commodity exchange trading for the top ten commodity exchanges in 2012 are given in *Table 5* and *Figure 6*.

It is notable that Russia's Micex-RTS (as the Moscow Commodity Exchange is referred to on the FIA website) appears on this list and, moreover, with a positive dynamic. According to FIA statistics, the Micex-RTS is in the top twenty Energy Futures and Options Contracts

(Brent Crude Oil Futures, ranked 16th), the top twenty Equity Index Futures and Options Contracts (RTS Futures, ranked 6th) and also in the top twenty Foreign Exchange Futures and Options Contracts (ranked 10th with Euro/US dollar Futures).

According to FIA statistics, the futures and options market did not do well in the first half of 2012. On the 84 global commodity exchanges, 10.2% less contracts were traded and/or cleared than in the same period in 2011.

The top ten commodity exchanges did not show any major change in participants. In terms of the volume of contracts traded and /or cleared almost all of them, with the exception of BM&FBovespa, the CBOE Group and Micex-RTS, slowed down their turnover. Positive movement was seen in the trading of futures and options contracts for precious and non-precious metals and energy. The remaining commodities showed negative growth. Breakdown by the region shows certain fluctuations, but apart from in Latin America the downward trend prevails. These were the major trends in commodity exchange volumes during 2012.

Commodity exchanges have evolved from local markets trading physical commodities to high-liquidity international markets trading futures and forward contracts. They are an excellent example of a self-regulating market institute and have become an integral part of the production and financial operations of a vast number of economic entities. Whilst maintaining their original characteristics – ensuring transparency of the trading process and competitiveness in the concluding of transactions – commodity exchanges have improved technically and in terms of the number of different operations performed and contracts handled. The following section deals with the trends which shape the future developments in the commodity markets worldwide.

3.1. Current trends in the development of organised commodity trade

One of the main international trends today is the reduction in the number of commodity exchanges and the merging of specialised exchanges into universal commodity exchanges. For example, a recent series of mergers created one new exchange from several American commodity futures exchanges which had been operating independently. Most of the mergers were pursued to increase the financial competitiveness of the commodity exchanges in the face of European competition and to offer institutional and commercial clients lower servicing costs. Europe's electronic trading was seen as less costly than the open outcry trading system prevailing in the US, in which all bids are made publicly.

One of the biggest changes was the creation of the CME Group from the merger of the Chicago Mercantile Exchange (CME), the Chicago Board of Trade (CBOT) and the New York Mercantile Exchange (NYMEX). The CME Group is now the world's largest commodity exchange in the volume of futures traded and offers its services at highly competitive rates. The new, fully electronic Inter Continental Exchange (ICE) was created in the US in 2000.

Commodity exchange mergers have also taken place in Europe and Asia. Larger exchanges acquired their smaller counterparts, and smaller exchanges merged to protect themselves from potential takeover. This trend is likely to persist. Once enlarged, commodity exchanges become ever more integrated into the international market. *Table 6* shows the important mergers and takeovers that have taken place over the last two decades.

Table 6 .

Important mergers and takeovers of commodity exchanges (1994–2012)

Period	Commodity exchanges and processes	Result
North America		
August 1994	Merger of the largest commodity exchanges in New York: NYMEX and Commodity Exchange Inc. (COMEX)	Creation of the New York Mercantile Exchange, the world's largest commodity exchange trading derivative instruments for oil and natural gas, precious and non-ferrous metals, electricity, etc.
June 1998	Merger of Coffee, Sugar & Cocoa Exchange Inc. (CSCE) and New York Cotton Exchange (NYCE) and its subsidiary structures Citrus Associates (the division for trading citrus product instruments), FINEX (financial division) and the New York Futures Exchange	Creation of the New York Board of Trade (NYBOT), handling instruments for trading agricultural products, currency, financial instruments and indices. NYBOT also becomes the largest commodity exchange for trading sugar derivatives
November 2001	Foundation of joint enterprise OneChicago LLC by the Chicago-based CBOE, CME and CBOT exchanges	Creation of a single Chicago commodity exchange for the futures trading of a range of securities and stock indices with a narrow allocation base. Members of the CBOE, CME, and CBOT commodity exchanges are also members of OneChicago
November 2003	Agreement to create the CME/CBOT Common Clearing Link	CME Clearing House to provide clearing and associated services on CBOT-traded instruments for the Chicago Board of Trade (CBOT)
January 2013	<p>In little more than a decade, the Intercontinental Exchange has grown from a start-up focused on the US energy and gas markets to a multinational company trading almost all types of assets capable of influencing global derivative markets</p> <p>The ICE has since acquired the International Petroleum Exchange, New York Board of Trade, the Winnipeg Commodity Exchange, The Clearing Corporation and the Climate Exchange, uniting and integrating them into a complex of markets and clearing houses.</p> <p>In one of its most recent and most ambitious deals, ICE is attempting to purchase NYSE Euronext (parent company of the New York Stock Exchange and icon of the US stock markets) and LIFFE, the second largest European futures commodity exchange. Approval by the regulator and shareholders of this merger will make ICE the leading force in futures and options trading on the % rate index and on cash equities markets.</p>	
Latin America		
May 1991	Merger of the Bolsa de Mercadorias de Sao Paulo (BMSP), Brazil's first commodity exchange, with the Bolsa Mercantil&de Futuros (BM&F) futures trading commodity exchange	Creation of the Bolsa de Mercadorias&Futuros (BM&F) joint commodity-futures exchange
June 1997	Merger of the Bolsa de Mercadorias&Futuros, BM&F commodity-futures exchange (BM&F) with the Bolsa Brasileira de Futuros – (BBF) futures stock exchange	Creation of the Bolsa de Mercadorias&Futuros (BM&F) commodity-futures exchange (BM&F), the largest forward market commodity exchange in Latin America and one of the top ten Derivative Exchanges
2008	Merger of Brazil's BM&F commodity-futures exchange and the Bovespa stock exchange of São Paulo	Merger to create BM&FBOVESPA
Europe		
1992	Merger of LIFFE with LTOM London Stock Exchange options market trading house	Diversification transforms LIFFE into one of the largest commodity futures exchanges in the world. LIFFE was renamed the London International Financial Futures and Options Exchange and therefore retained its abbreviated title
1996	Merger of London Commodity Exchange (LCE) with LIFFE	
December 1996	The German Commodity Exchange (Deutsche Boerse AG) and the Swiss Exchange signed a protocol merging their subsidiary commodity futures exchanges: Germany's Deutsche Termin Boerse (DTB) futures exchange and the Swiss Options and Financial Futures Exchange (SOFFEX). The merger of DTB and SOFFEX was finally completed in 1998. The merger also created the EUREX Clearing subsidiary clearing house	Creation of EUREX, Europe's largest commodity exchange for derivative instruments. EUREX has since become the world's leading commodity exchange in terms of trading volume

Period	Commodity exchanges and processes	Result
September 2000	Merger of the Paris Bourse SBF SA, Amsterdam Exchanges and Brussels Exchanges	Creation of the single European commodity exchange EURONEXT NV, integrating the trading, clearing and settlement systems for the stock, futures and commodity markets of all three exchanges. EURONEXT operates on three commodity markets: Euronext Amsterdam, Euronext Brussels and Euronext Paris
Asia Pacific		
December 1998	Merger of the Kuala Lumpur Commodity Exchange (KLCE) and its subsidiary, the Malaysia Monetary Exchange (MME)	Formation of COMMEEX, the single Commodity and Monetary Exchange of Malaysia
Intercontinental takeovers and alliances		
June 2001	Takeover of the London Commodity Exchange IPE by the American Intercontinental Exchange (ICE)	Emergence of a global electronic trade platform trading energy derivative instruments. Creation of a serious competitor to NYMEX
June 2003	Signing of a memorandum of understanding extending cooperation between NYMEX and the Tokyo Commodity Exchange (TOCOM)	Under the terms of the memorandum, the commodity exchanges granted participants access to all trading instruments and allowed them to cooperate on the development of new products in new areas of activity
February 2004	Agreement between the Board of Trade Clearing Corporation (BOTCC) and Eurex US, the American subsidiary of the Eurex commodity exchange, on the provision of services by the clearing corporation	Creation of a US futures market alliance between one of the world's largest clearing houses – BOTCC – and the world's largest commodity futures exchange – Eurex. Entry of Eurex into the US market
2007	Merger of NYSE with the Euronext group of European commodity exchanges	Merger
2008	Nymex bought out by CME Group	Takeover
2011	Negotiations on acquisition of Chi-X Europe by the US alternative trading platform BATS Global Markets in a deal worth around \$300 million. According to Thomson Reuters, Chi-X Europe and BATS Europe, the European subdivision of the BATS Global Market, was set to take 22.9% of the combined European market, with the Deutsche Boerse/NYSE receiving 29.7% and the LSE 23.4% (Koksharov, 2011)	The commodity exchanges withdrew from the deal on February 2, 2012
2011	NYSE Euronext and Deutsche Boerse merge to create the largest commodity exchange for derivatives trading. The European Commission came out against the merger and blocked the deal on February 15, 2011 This was the second time that a plan to merge Deutsche Boerse and NYSE Euronext had failed. The first negotiations were conducted in 2008 following the NYSE's purchase of France's Euronext trading platform. That deal also foundered	Merger negotiations did not take place
2011	Russia's MICEX (Moscow Interbank Currency Exchange and RTS (Russian Trading System) unite to form the Moscow Commodity Exchange	Merger
December 7 2012	The Hong Kong Stock Exchange (HKEx) completed its acquisition of all ordinary shares issued on the London Metal Exchange (LME). The acquisition was reported by the Xinhua agency. For over 135 years, the LME has been the main depository for buyers of metals, including copper, aluminium and nickel, consumption of which is greater in China than in any other country. The acquisition looked promising given the record levels of trading on the London Commodity Exchange. Trading in September was at its highest level since records began. In September alone, over 14 million contracts were signed. The volume of transactions carried out on the LME since the beginning of the year exceeded that of the same period in 2011 by 8%. In 2011, over 146 million contracts amounting in total to \$15.4 trillion were concluded on the LME	HKEx issues 65.7 million new shares to be distributed among independent professional and institutional investors, thus attracting 7,753 billion HK dollars (\$1 billion). These shares represent around 5.71% of the shares already issued

Source: Solovyov, 2004

Another important tendency is the commodity market's changing role and function to that of a financial institution. The commodity market has been transformed from a market dealing in goods to a market dealing in rights to goods. The "universalisation" of commodity markets and the diversification of their trading instruments have led to a significant reduction in the number of transactions involving physical commodities and a lowering of the value of these transactions as a percentage of total commodity market turnover. The transition from trading in real goods to trading in their derivatives has altered the primary function of the commodity exchange from organising the sale of commodities to servicing trading operations (Samarin, 2007). This trend gathered significant momentum after the start of the new millennium in 2000 and its effects are likely to be far-reaching.

The idea of a forward market is fundamental to classic economic theory and is seen to have a number of important functions. These include price risk control, the provision of information for commercial agencies, speculation and the creation of new financial instruments (Mikhailov, 2000). Today, however, the volume of trade in derivatives (futures, options, commodity swaps, etc.) significantly exceeds the volume of trade in basic commodity market assets (Moryi, Maqsimchuk, 2012). In a number of commodity groups, e.g., crude oil, petroleum derivatives, precious metals and grain, this is leading to changes in the price-setting mechanism. The traditional method of setting price on spot markets based on the supply and demand of real producers and consumers is being distorted. In many cases, prices are now being set on forward markets, where the financial strengths of the major investment houses are pitted against each other in an attempt to pursue speculative ventures based on the predictions of their own and other independent analysts. The hedging operations carried out using the financial resources of real producers and consumers, financial assets and products have also given way to poorly regulated, speculative trading operations undertaken by the many offshore hedge funds, trusts, etc., able to operate with excessive amounts of financial capital. Such a situation calls for the introduction of stricter controls, although it is possible that once regulation has been introduced, the trend described above will begin to weaken; at this moment in time, however, the futures market is in a dominant position with regard to the spot market.

According to researchers, the trends that now typify the development of the sector as a whole are technological development and the growth in the number of commodity market participants. The development of commodity exchange trading globally has led to a significant increase in the number of commodity market participants and a broadening of the spectrum of economic entities trading on the markets. Traditional derivative market participants have now been joined by governments, state financial institutions, international financial companies, transnational corporations, banks, insurance societies, pension funds and private investors. This is due to changes in legislation in developed countries, which have legalised innovative commodity exchange mechanisms (Samarin, 2007).

The transition from the "open outcry" system of traditional commodity exchange trading to electronic trading has been made possible by advances in communications technology and their introduction to market trading practices. The new commodity exchanges created at the end of the 20th century (see ICM above) are all oriented towards electronic trading. The first commodity exchange with a fully electronic trading system was the New Zealand Futures and Options Exchange, which opened in 1985. According to the Chairman of the Chicago Chamber of Commerce, D. Brennan, the global volume of electronic trade doubled

Table 7.
Volume of commodity futures by selected commodity exchanges

Stock Exchange	Volume traded (number of contracts)		Notional value (\$ millions)		Open interest (number of contracts)		Number of trades	
	2011	2010	2011	2010	2011	2010	2011	2010
BMS&BOVESPA (Agricultural futures)	2 040 475	2 275 100	41 035	35 983	36 837	568 761	492 817	
CME Group (Agricultural, energy and metal futures)	608 579 048	541 540 557	47 168 617	33 625 981	25 866 122	328 799 168	275 343 005	
Dalian Commodity Exchange (Agricultural futures)	289 047 000	403 167 751	2 616 862	3 084 985	1 580 328	NA	NA	
Shanghai Futures Exchange (Agricultural, energy and metal futures)	308 239 140	621 898 215	6 738 220	9 133 773	1 070 010	NA	NA	
Tokyo Commodity Exchange (Agricultural, energy, metal and commodity index futures)	31 670 031	27 636 367	1 210 782	808 335	323 801	NA	NA	
NYSE LIFFE (European markets) (Agricultural futures)	17 265 995	14 133 913	406 510	304 149	642 029	5 145 379	3 477 061	
RTS (Agricultural, energy and metal futures)	36 764 175	17 784 436	57 081	18 296	79 845	2 793 293	936 407	
Budapest Commodity Exchange (Agricultural futures)	5 318	6 854	177	166	221	1 452	1 759	
Eurex	58 755	53 407	891	528	6 562	17 491	16 961	
Zhengzhou Commodity Exchange (Agricultural futures)	406 439 457	495 904 984	NA	NA	935 600	NA	NA	
ICE Futures Europe (Energy futures)	257 993 927	210 402 962	NA	NA	2 928 494	NA	NA	
Multi Commodity Exchange of India (Agricultural, energy and metal futures)	346 192 367	197 206 801	NA	1 905 357	NA	NA	NA	
NYSE Euronext (US markets) (Metal futures)	3 655 545	3 730 746	NA	NA	9 570	13 574	NA	

Source: <http://www.world-exchanges.org/statistics/derivatives>
Note: NA – data not available

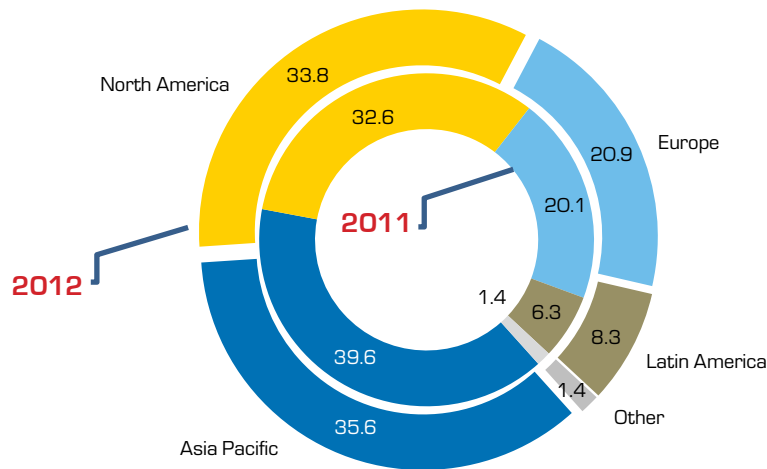
between 1995 and 1998, whilst the volume of “auction” trading fell by 17%. This trend is set to continue.

During the mid-1990s, commodity exchanges on which derivatives are traded began to appear in developing countries and in the countries of the former Soviet Union. This broadened the geography of commodity market trading. However, the major commodity exchanges concentrated themselves in the world’s leading financial centres, due to the presence in those centres of a developed banking infrastructure, capital, an effective system of regulation and better investor protection – in other words, a favourable environment for commodity market activity.

The US is the leading futures trading nation. It gained this leading position in part thanks to the Commodity Futures Modernisation Act of 2000.

Figure 7.
Global Futures
and Options
Volume by Region
[% , 2011 and
2012]

Source: FIM, 2013



The range of commodities whose derivatives are traded on the commodity exchange is increasing. During the 1960s and 1970s, futures contracts markets expanded to include more than 20 new commodities. These included timber, gold, silver, palladium, oil, propane, orange juice concentrate, various kinds of meat and meat products. New commodities are sometimes brought onto the contracts market through deregulation of the given resource market – electrical energy, for example. This is the case in most European countries and in the US. The inclusion of new industrial raw materials (crude oil, diesel, nickel, aluminium, timber, plywood) alongside traditional ones has led to increases in the number of commodities and in the volume of commodity exchange trading. As a result, agricultural and forestry products account for a smaller proportion of all the exchange commodities, although these goods are still ranked very highly. Nowadays, a brief glance at the list of exotics is sufficient proof that just about any type of commodity can be traded.

Probably the most important trends are the ongoing unification of commodity exchange organisation on a global scale and changes to the methods of regulating commodity exchange activity. The global unification of commodity exchange organisations is taking place against a backdrop of universal trade and financial liberalisation. Unification is epitomised by the currency in which forward commodities are quoted – the US dollar. Although

supervisory and control functions rest with the state, many powers are now being transferred to trading organisers and self-regulating bodies in the sector. However, the recent financial crisis and the scandals coming to light in the financial sector may prompt a return to stricter regulation.

In the context of the trends described, experience globally shows that the commodity trading has little bearing on real economics and is increasingly becoming part of the financial market. Economic globalisation actually promotes the unification of commodity exchanges. The international entities created are able to establish global commodity prices. Unification also leads to the appearance of new commodity exchanges, which in turn accelerate the process of global economic integration. Recently, the number of traders has significantly increased due to changes in legislation and technological advances that have profoundly altered the attributes of the commodity exchange.

Having examined issues of development, regulation and turnover in the trading of commodity market futures and options, we go on to look at what is happening in the CIS.



4. The Main Phases of Development of the Commodity Exchanges in Russia and Kazakhstan

The events which led to the birth and development of commodity markets in Russia and the new republics following the collapse of the USSR have been well studied and documented in the works of that period (e.g., Shatalin, 1990; Manevich, 1991).

The processes of disintegration had a profound political and economic impact. The collapse of the single economic area and the introduction by the newly created states of their own currencies and customs borders destroyed old, traditional cooperative links. The economies of all these countries were in crisis at the beginning of the 1990s, with zero economic growth, falling industrial production, growing budget deficits, rising inflation and widespread commodity shortages.

The industrial enterprises of the CIS member states found themselves in entirely new economic circumstances. Centralised supply was swept away with the old system and traditional cooperative links were broken. Commercial relations moved towards a system of free price setting. For producers, the transition to a market economy required economic structures that could support the creation of new cooperative links and new price orientation. In other words, commodity markets became not only a reality, but a necessity for the industrial and agrarian sectors. Markets also required participants who were willing to turn their capital into goods and materials at a time of commodity shortage and growing inflation.

The excessive build-up of unsold stock in company warehouses – goods that could be sold at market prices through a central market – was another factor militating for the creation of a commodity exchange. Moreover, the exchanges themselves became entities into which surplus cash could be invested. Hence the commodity exchanges which began to appear in the early 1990s helped resolve these issues.

4.1. Russia

Economic reform and the privatisation of state property at the beginning of the 1990s gave rise to a new property-owning class, which included many medium to large businesses. Tens of thousands of new shareholder companies, cooperatives, partnerships and public- and privately-owned companies were formed.

The actively developing production sector demanded new trading markets and market institutions; in a free wholesale market new and existing companies sensed a sharp rise in demand for raw materials and finished products with no price controls.

The Gosbank and Vneshekonombank currency auctions and the Gossnab commercial centres, which sold technical products by auction at the end of the 1980s, formed the basis of the future commodity exchanges. The creation of the Moscow Commodity Exchange and the All-Russia Goods and Raw Materials Exchange in the first half of 1990 marked the start of a commodity exchange boom in the Russian Federation. Russia rocketed into first place worldwide in terms of the number of active stock exchanges. Moscow very quickly

Table 8.

Main phases of commodity exchange development in Russia

Stage	Main characteristics	Main events
1990–1991	<p>A period of rapid growth in the number of commodity exchange structures and brokerage companies (see Figure 9)</p> <p>Commodity exchanges, like companies, are created to make a profit.</p> <p>Initially, the atmosphere on the Russian commodity exchanges is more akin to stalls on a local market than to a modern commodity exchange trading floor.</p> <p>The commodity exchange functions as a centre for facilitating trade in a very wide range of goods and materials.</p> <p>Commodity trading is almost exclusively based on transactions involving real cash commodities.</p> <p>This is a “hypertrophied” commodity exchange with an over-abundance of brokers and intermediaries.</p>	<p>At this early stage, manufacturing companies are in great need of a free wholesale market to purchase raw materials and sell finished products at uncontrolled prices. The establishment of new industrial relationships and new sales outlets are equally important.</p> <p>An unstable macroeconomic environment, uncertainty in economic relations and wholesale market prices fixed by the state encourage commodity exchanges to become more general.</p>
1992–1994	<p>A period of reorganisation on the Russian commodity exchanges and decline in trading activity</p> <p>Exchange trading is “freed” from commodity exchange structures and “quasi-commodity exchanges”. Competition between commodity exchanges and off-exchange structures intensifies.</p> <p>Refinements to exchange trading procedures gather momentum coupled with a rapid increase in the rate of commodity market integration and concentration.</p> <p>Specialised domestic commodity exchange trading begins to emerge. Many exchanges refuse to trade a wide range of goods and resources.</p> <p>The first forward contracts are traded. Futures trading is initially confined to commodities such as oil and oil derivatives, grain and non-ferrous metals.</p>	<p>1991 and 1992 sees the adoption of federal laws and regulations bringing the legal status of Russian exchanges into line with international standards. At this stage, stock markets are more in line with global practice than commodities markets. This tendency continues.</p> <p>The beginning of 1992 is a milestone for the Russian exchange market. Three powerful factors come into effect:</p> <ul style="list-style-type: none"> • introduction of free pricing; • new commodity exchange legislation; • increases in the tax payable on brokering activities. <p>The advantages of free pricing are made available to all market participants. The stock exchange loses its exclusive rights and monopolistic position; profitability decreases.</p> <p>Together with price liberalisation and a tightening up of commodity exchange regulation, the tax burden on commodity exchanges also increases. As a result, commodity exchange trading decreases sharply, trading shifts to off-exchange markets and brokering activities become much less attractive.</p> <p>The forward trading of grain and cotton begins on the Moscow Commodity Exchange (MCE) and the Moscow Chamber of Commerce organises futures trading instruments for the US dollar.</p>

Stage	Main characteristics	Main events
1995–1996	<p>The introduction of electronic commodity exchange trading</p> <p>The commodity exchange is transformed from a “local market stall” where real goods are sold into a computerised derivatives market.</p> <p>Virtual trading replaces traditional commodity exchange trading and provides market participants with automated purchase/sale and settlement via remote terminal.</p>	<p>Wholesalers refine their trading practices, establish solid commercial partnerships and start to abandon trading floors. Exchange members begin operating on off-exchange markets. Only those commodity exchanges unaffected by real cash flows and able to trade in futures contracts survive. By the end of 1993, the number of commodity exchanges has decreased by one third and by the end of 1996 has fallen to some 40% of the 1992 figure. By the late 90’s, many of those which survive have already closed their floors to professional brokers, speculators and hedge-fund operators.</p> <p>The Moscow Commodity Exchange, the Moscow Non-ferrous Metals Exchange and other Russian exchanges begin to adopt electronic trading systems. Virtual exchanges such as Grain On-line, the Russian Metallurgy Sector (rusmet.ru), the Ural Metals Market and a number of other electronic commodity exchange sites are created.</p> <p>Optimism among electronic commodity exchange market organisers during the late 1990s that the volume of trade would increase now fades.</p> <p>The transformation of the Russian commodity exchanges into an online trading system coincides with similar changes worldwide; trading on the leading exchanges increases due to improvements in settlement procedures and remote access networks. With greater liquidity and increased trading volumes, international commodity exchanges are becoming more attractive for both Russian and foreign market participants.</p> <p>Reduction in the local value of domestic commodity exchanges and increased competition leads to a fall in the number of foreign investors, buyers and sellers on Russian commodity markets and a reorientation of Russian investment activity on oil, agricultural and metal markets towards global exchanges.</p>
1996–2000	<p>A period of consolidation and integration on the commodity exchange markets and a decline in the volume of trading</p> <p>Regular trading on the futures markets</p>	<p>By the beginning of the new millennium, commodity exchange trading has undergone a qualitative change, due to the introduction of electronic trading (see Figure 12).</p> <p>Commodity exchanges unable to make the necessary improvements to their trading process opt for restructuring. The entire corporate structure of these exchanges is dissolved and replaced by groups of holding companies. The Russian Foodstuffs Exchange, for example, reorganises into the Chekoviy Investment Privatisation Fund, the Russian Food Bank and a financial/industrial group.</p> <p>Mergers represent another way of reorganising.</p> <p>For example, a merger involving the Moscow Universal Exchange of Secondary Resources (MUBVR), the Konversiya commodity exchange and the Forestry Exchange, leads to the establishment of the Moscow Chamber of Commerce. RUISbirzha merges with the Moscow Commodity Exchange. Many commodity exchange companies enter similar arrangements</p>
2000–2011	<p>The introduction of electronic exchange trading in commodity futures on Russian trading floors and the use of exchange pricing for gas and electricity</p>	<p>A commodity exchange trading in gas opens in Moscow in November 2006 and Arena – a Moscow “energy” exchange – begins trading in July 2007. In 2010, the government decides to support grain trading on the commodity exchange. The decision was prompted by a severe drought and speculation which inflated prices for grain and cereals (see Figures 10, 11, 12). This allows the commodity exchange to become an institution protecting consumer rights through price competitiveness, eliminating the need for a long line of middlemen.</p>

Source: <http://vadim-galkin.ru/>, Stages in the development of the commodity market in Russia; September 29, 2011

became the global commodity market capital; 40% of all the world's commodity exchanges worldwide were located in Russia. Since 1993, the number of commodity markets has been decreasing (see Figure 9).

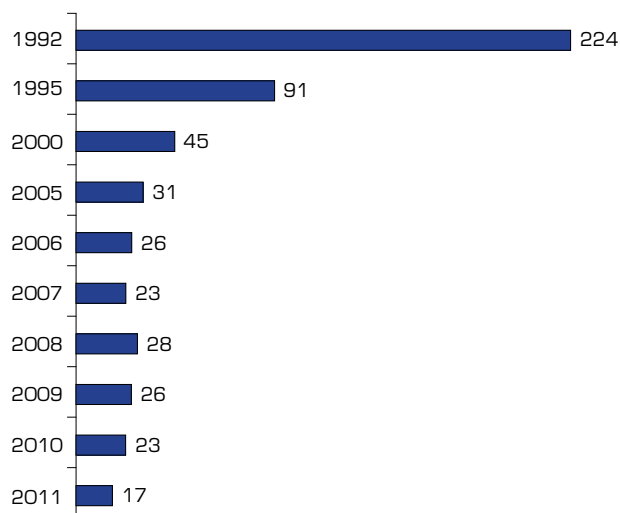


Figure 8.

Number of exchanges and commodity floors on the commodity and stock markets

Source: FSSS, 2012; FAS, 2012

The resurgence of Russian commodity exchange activity became one of the defining moments in the transition of the centrally planned economic system to the market system. Initially, due to the collapse of the centrally controlled supply system, stock exchanges took on the role of commodity exchange. Investment, insurance and brokerage firms, trading houses and commercial banks grew up around commodity exchange structures.

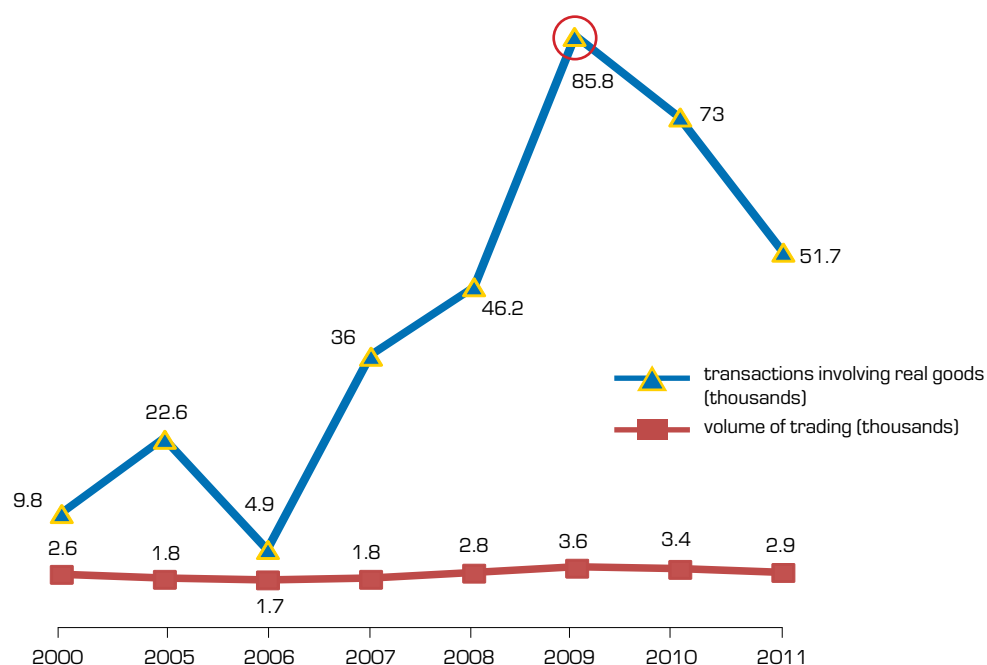


Figure 9.

Primary activities on Russian commodity markets (2000–2011)

Source: FSSS, 2012; FAS, 2012

Figure 10.

Commodity exchange turnover from transactions involving real goods, not including futures transactions (\$ million)

Source: FSSS, 2012; FAS, 2012

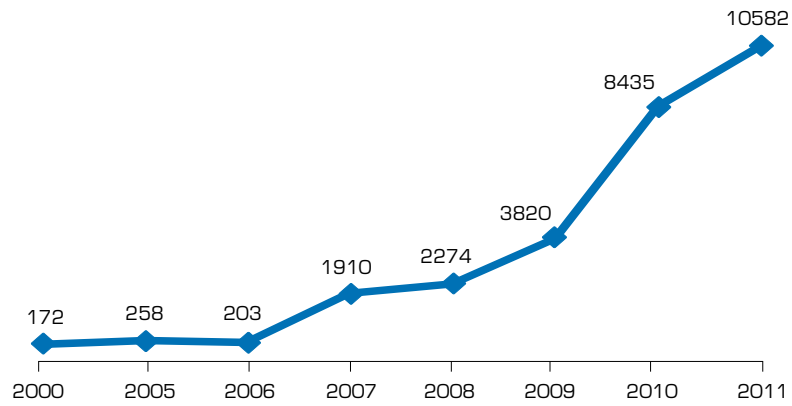
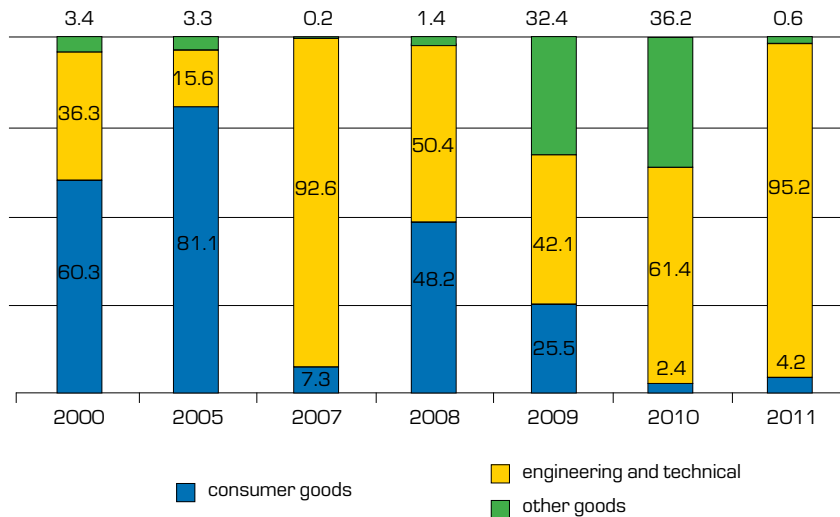


Figure 11.

Exchange turnover by type of operation (%)

Source: FSSS, 2012; FAS, 2012



The commodity markets attracted capital, which was invested in business development and the creation of an information infrastructure. One of the commodity exchange's most important contributions was the formation of the country's first cadre of professional businessmen.

Moreover, commodity exchange trading procedures became more organised and legislation on commodity exchange activity was established in line with international standards (Demchuk, 2006). Alignment with global standards, the application of foreign expertise to the working practices of the commodity exchange institutions and commodity market regulators and the proximity of highly developed and competitive foreign markets helped the Russian commodity market, despite its short history, develop in the mould of commodity markets in developed countries.

4.2. Kazakhstan

The prerequisites for the emergence of commodity exchanges and the development of goods and raw materials markets in Kazakhstan are similar to those of Russia. It should be noted

that, in the early stages of their development, commodity markets in CIS countries were trading not only on their own floors, but also with other commodity exchanges in Central Asia and Kazakhstan (15 exchanges), the Siberian Ring consortium (16 exchanges in Russia), the Commodity Exchange Association of North West Russia and the Baltic (14 exchanges) using real time modem and selective communication facilities.

Table 9.
Main events in the development of commodity exchange trading in Kazakhstan

1991	June 13, 1991 – adoption of a special law on commodity exchanges in the Republic of Kazakhstan. Stock and commodity exchanges begin to emerge, gaining organisational experience and conducting open and closed exchange trading in a wide range of goods and services, real estate and securities.
March 1994	The Presidential Decree of the Republic of Kazakhstan of March 20, 1994; no.1604 “On Commodity Exchanges”, supersedes the law adopted in 1991. Commodity exchanges, their objectives and primary functions are now defined and extended.
April 1995	Exchange specialisation begins, with separation into commodity and currency/ stock exchanges. New Presidential Decree no. 2170 of the Republic of Kazakhstan of April 7, 1995 “On Commodity Exchanges” comes into force and changes control of the market infrastructure. Under Resolution no. 1035 of the Cabinet of Ministers of the Republic of Kazakhstan of July 28, 1995, grain becomes an exchange commodity, complementing Law no. 2170 “On Commodity Exchanges” of April 7, 1995. The grain exchange is active from 1995–1997. The list of exchange commodities is extended to include agricultural products, skins and hides, animal and industrial products (including petroleum derivatives, wood, and ferrous and non-ferrous metals).
1996	Introduction of commodity exchange licensing. The Commodity Exchange Committee is legally appointed as the regulatory body, answerable to the Cabinet of Ministers.
December 1997	Trading activity declines due to the adoption of regulations excluding industrial products from the list of exchange commodities. Trading in other groups of exchange commodities is regarded as non-binding, especially in respect of exports.
May 2002	Commodity exchange activities resume due to the state procurement of exchange commodities in open trading, in accordance with Republican Law no. 321 “On Public Procurement”, adopted on May 16, 2002.
March 2004	Resolutions adopted to halt the decline in market activity coupled with a fall in the number of exchanges reduce the number of exchange commodities (see Picture 13).
2007	Head of State, Nursultan Nazarbayev, orders that measures be taken to develop the exchange market and the exchange market sector.
Autumn 2008	The exchange trading of grain in Kazakhstan virtually ceases in 2008; according to Ministry of Agriculture statistics, only 500,000 tonnes of grain were sold through the existing commodity exchanges.
December 9, 2008	JSC Commodity Exchange Eurasian Trading System (ETS) is created by order of the President of Kazakhstan, Nursultan Nazarbayev, and is 40% state-owned. Other participants are JSC Regional Financial Centre of Almaty and OJSC RTS Stock Exchange (Russian Trading System). The main purpose of this commodity exchange is to keep major commodity group prices transparent, reduce brokering costs related to the buying and selling of goods and ensure fair prices for buyers and sellers. Exchange partner, RTS, one of the leading electronic trading platforms in Russia, contributes to ETS charter capital a range of software products used for futures and spot-market trading. ETS is now well placed to organise trading in line with international standards.
March 2009	Bidding on the ETS agricultural market begins on March 30, 2009. The trading floor hosts a wide range of players, represented by professional brokers trained by the exchange. The floor attracts participants from Turkey, Tajikistan, Iran and Uzbekistan. ETS has an up-to-date structure, including clearing and settlement facilities and is able to conduct electronic trading on a wide range of commodities. ETS is the only exchange in Kazakhstan conducting electronic trading to modern exchange industry standards.

May 2009	<p>The new law no.155-IV of the Republic of Kazakhstan of May 4, 2009 "On Commodity Exchanges" replaces the law of April 7, 1995 and establishes new principles and approaches to exchange trading.</p> <p>The law "On Commodity Exchanges" enshrines the right of the state to approve the list of exchange commodities and the minimum lots traded on the commodity exchange.</p> <p>This law regulates the activities of the commodity exchanges and is designed to eliminate omissions in previously adopted legislation. The new law introduces concepts such as brokers, dealers and clearing and settlement centres. It also opens up opportunities for the introduction of modern trading technologies (e.g., online trading) and introduces a system of risk management.</p>
November 2009	Resolution no.1942 of November 26, 2009 establishes a licensing system for commodity exchange activity and the qualifications required to engage in commodity exchange operations and brokering.
December 2009	<p>Model rules for exchange trading are approved by Resolution no. 2042 of the Government of Kazakhstan on December 8, 2009.</p> <p>This law is also aimed at improving existing legislation on the state regulation of agriculture and, in particular, the laws entitled "On Grain" and "On State Regulation for the Development of Agriculture and Rural Settlement". These amendments and additions to existing legislation are meant to increase state financial support and strengthen government regulation of the food market and the exportation of agricultural products.</p>
April 2011	Government of the Republic of Kazakhstan Resolution no. 37 of April 6, 2011 establishes the list of exchange commodities and the minimum lots traded by the commodity exchanges. The list includes potatoes, wheat, sugar, coal, cement and other commodities.
December 2012	Resolution no. 1653 of December 21, 2012 establishes required qualifications for commodity exchange operators, commodity exchange brokers and dealers.

In Kazakhstan, participation in commodity market trading is still not at the levels seen in the West and in Russia. Most domestic commodity markets are still developing and improving. However, given Kazakhstan's enormous potential in the agrarian and raw material sectors, the commodity market is seen as the most advantageous system for this country.

According to statistics compiled by A. Kazybaevy, Chairman of the MERT Committee for Trade in Kazakhstan, the commodity exchange has been actively developing over the past three years. In 2011, total commodity exchange turnover amounted to around \$3 billion and trading activity on the commodity exchange amounted to 5% of wholesale turnover, compared with just 1% in 2010. Kazakhstan aims to increase trading activity by introducing measures to ensure transparency in the pricing of strategic commodities (Shaternikova, 2012).

In recent years the country has clearly made substantial efforts to develop commodity exchange mechanisms, but it would be somewhat premature to claim that there has been a wholesale modernisation of the system. Legislation has not been amended swiftly enough and legal standards have not always achieved the intended result.

Nevertheless, the creation of the Eurasian Trading System commodity exchange in 2008 and the adoption of the "Law on the Commodity Exchange" in 2009 have laid the foundations for a new and dynamic commodity exchange and represent a significant step forward for commodity exchange trading in Kazakhstan (see Figures 14, 15).

Similarities in the development of the Russian and Kazakh commodity exchanges are significantly outnumbered by the differences. One inherent similarity is the slow growth in commodity exchange activity, which has been blamed on state intervention. In Russia,

this intervention took the form of stricter commodity market regulation and tax increases coinciding with price liberalisation in 1992. In Kazakhstan, as the commodity market evolved, continual legislative amendments meant the necessary “rules of the game” were not established. The situation in both countries is characterised by increased intervention in commodity market activity pursued by the state at the expense of offering any real support.

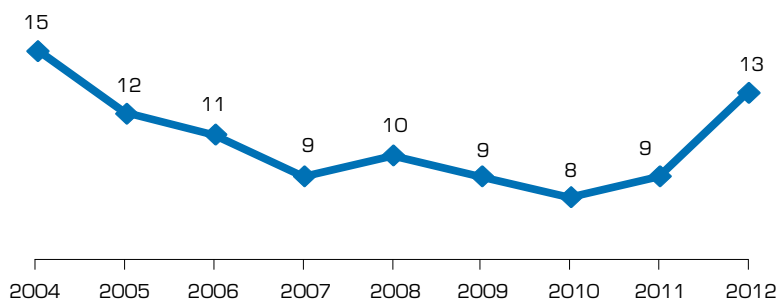


Figure 12.

Number of commodity exchanges in Kazakhstan

Source: <http://www.stat.kz/digital/torg/Pages/default.aspx>

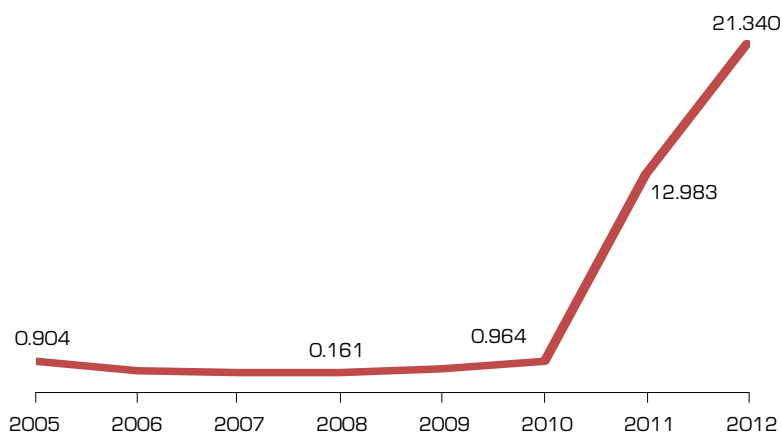


Figure 13.

Volume of exchange trading

Source: <http://www.stat.kz/digital/torg/Pages/default.aspx>

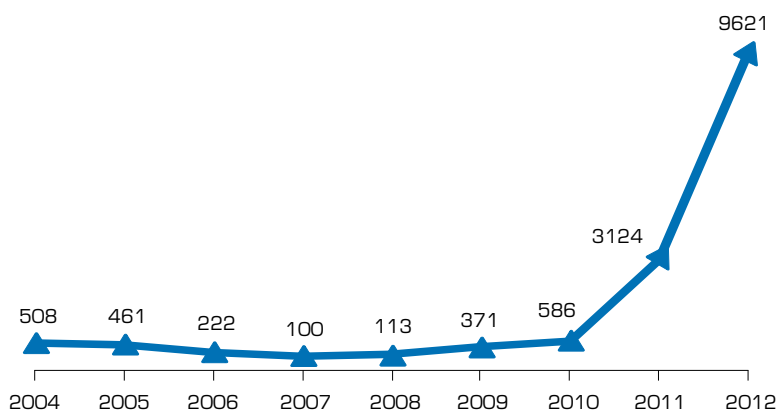


Figure 14.

Exchange turnover from transactions (\$ million)

Source: <http://www.stat.kz/digital/torg/Pages/default.aspx>

Another similarity between the countries is the degree to which commodity markets lag behind their stock markets in terms of organisation and interaction. State participation in the establishment and control of a commodity market is fundamental. But although this state participation is evident in Russia, it was mostly absent in Kazakhstan, where the first commodity exchange created with state participation appeared only in 2008.

Just as Russian commodity exchanges were beginning to adjust to the changing economic environment and were forging ahead with electronic trading for forward contracts, in Kazakhstan these processes had stalled at the real commodity trading stage. Moreover, the Kazakh government decided to stimulate trade by introducing a list of commodities that could only be traded according to established procedures.

There have been occasions in the history of the Kazakh commodity exchange when the creation of a corn exchange would have improved grain trading and changed the landscape of this sector significantly, allowing the potential of the commodity exchange mechanism to be fully realised. But in 2008, grain trading on the Kazakh commodity exchange came to a virtual standstill.

Arguably one of the greatest differences between the development of commodity exchange trading in Russia and Kazakhstan has been the patent lack of interest in developing the Kazakh market. Transactions on the commodity markets had long meant little more than getting a stamp for contracts negotiated outside the exchange, marking the contract with yesterday's date and settling under auction-type conditions. The low level of organisation of the commodity markets made it virtually impossible to support Kazakh producers, irrespective of how well they organised their production and the actual cost of their products. Commodity exchange trading will inevitably be the mechanism through which the organisation of the Kazakh commodity markets is improved.

Market development, competition, the introduction of new instruments and electronic trading have all made the Russian market what it is today. Kazakhstan lags behind Russia in all these aspects, but the Kazakh market is growing and the outlook is good.

Table 10.

Comparative data on the commodity exchanges of Kazakhstan, Russia and Ukraine (2009 – 2010)

In other CIS countries, statistical committee data suggest that many problems still exist, but that commodity market activity in a number of CIS republics reflects the positive trends seen in Russia and Kazakhstan.

Source: Database of the CIS Statistical Committee on stock, commodity and currency exchanges

	Number of commodity exchanges operating at the end of the year		Number of transactions concluded during the year (thousands)	
	2009	2010	2009	2010
Kazakhstan	9	8	1.1	10.4
Russia	26	23	85.8	73
Ukraine	343	339	383	88

On February 14, 2012 the Kommersant Ukraine, referring to the Concept for Development of the Ukraine Commodity Market, reported that there were currently some 500 commodity markets in the country. However, the annual turnover of the commodity market fluctuates between 5 billion and 8 billion hryvnia – a sum approximately equal to total trade in a single session on exchanges such as the Chicago Commodity Exchange or the NYSE Euronext.

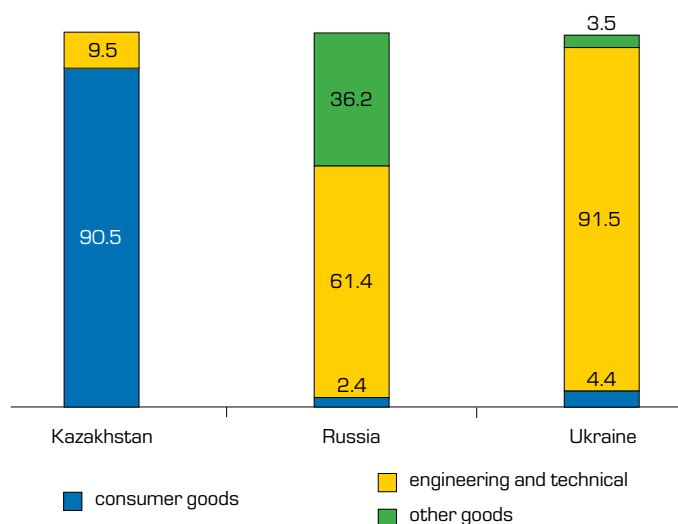


Figure 15.

Exchange turnover by type of operation (2010)

Source: database of the CIS Statistical Committee on stock, commodity and currency exchanges

In Kazakhstan, commodity exchange trading increased in 2010, partly due to the launch of the grain spot market on the ETS commodity exchange. In Kazakhstan, increases in commodity exchange turnover are accounted for by consumer goods. In Russia and Ukraine, engineering production accounts for the major share in turnover.

Commodity market development is on the reform agenda of practically all CIS countries. The results of studies undertaken jointly by the EDB and the IAE CIS will be discussed in the next section. A comparative analysis of state legislation in Russia, Kazakhstan, Belarus and Ukraine suggests that activity on the region's national commodity markets could increase if a single commodity exchange area is created.

5. Cooperation Between the SES Countries on Organised Commodity Markets

One outcome of the economic partnership between Russia, Kazakhstan and Belarus in the Customs Union (CU) has been the creation of a joint commodities market in the Single Economic Space (SES). This in turn has increased mutual trade between CU member states. The simplification of customs procedures has opened up opportunities for commodity exchange and helped to increase mutual trade between the member states. A logical next step would be to create a single commodity exchange area in order to resolve issues of cooperation between the countries on organised commodity markets.

The political weight brought to bear during the creation of the CU and SES is reflected in the ambitious deadlines for this enormous project. However, when the project was initiated on December 9, 2010, certain aspects essential to the effective functioning of the internal commodities, services and capital markets appear not to have been taken into account. In 2010, for example, during the setting up of the CU, a commodity exchange for agricultural products was proposed as part of an overall plan to create a single commodity exchange area for producers and consumers of agricultural products in Russia, Belarus and Kazakhstan (IDK Expert, CIS: Commodity Exchange Consolidation, February 22, 2010). However, the specific details of how cooperation on the raw materials markets would be structured were not properly worked out, which meant the project failed to get any response from potential participants and therefore never came into being.

In November 2011, the Commodity Exchange Society of the IAE CIS proposed the appointment of a committee to oversee the development of commodity markets. The eight members of the committee were appointed from the IAE CIS, the Belarus Universal Commodity Exchange (BUCE), the Moscow Interbank Currency Exchange, the Saint Petersburg International Commodity and Raw Materials Exchange, the Ukraine Interbank Currency Exchange, the Moldova Stock Exchange, the ETS Commodity Exchange and the International Commodity Exchange of Kazakhstan. The committee was given three main tasks: to develop a model for interexchange integration of the commodities markets in the

CIS and EurAsEC republics; to harmonise legislation regulating the national commodities markets; and to create an infrastructure for commodity market integration. The establishment of a specialised structure within the IAE CIS provided an opportunity to resolve the key issues of commodity exchange cooperation on the commodities markets, taking into account the interests and demands of the direct participants.

Although commodity exchange trading represents a relatively small proportion of the overall volume of commodity sales in the SES republics, the need for new types of commodity exchange in the region is pressing. In the SES member states – exporting countries with significant raw material and agrarian potential – the domestic commodity exchanges were responsible for price setting. The development of commodity exchange trading has focused attention on issues relating to the unification of commodity market regulation and the creation of an exchange trading infrastructure.

Meaningful discussion of potential cooperation between the SES member states on organised commodity markets cannot take place unless issues relating to raw material markets and barriers to interexchange cooperation are properly addressed. The EDB and IAE CIS investigated these issues in 2012 (see Unification of Commodity Exchange Legislation in the Republics of Belarus, Kazakhstan, Moldova, Uzbekistan, the Russian Federation and Ukraine).

Central to the research was a comparative analysis of SES and CIS member state regulation of national commodity markets (in Belarus, Kazakhstan, Moldova, the Russian Federation, Ukraine and Uzbekistan – hereinafter referred to as “the SES+”). The analysis prompted calls for legal provision for interexchange cooperation and the formation of an integrated commodities market in the SES+ member states, based on selected commodities (wheat, maize, diesel oil, 92- and 95-octane petrol, heating oil, dried milk and casein).

For the purposes of this report, the results of that study are presented in an abbreviated format only for the SES member states and Ukraine.

5.1. Member state legislation regulating organised commodity markets, market participants and standard exchange contracts and exchange commodity regulations and restrictions

State regulation of commodity exchange activity

A comparison of relevant SES+ national legislation was carried out with the aim of identifying barriers and moving towards an agreement on legal standards.

Country	State regulation of commodity exchange activities
Republic of Kazakhstan	<p>Government acts to regulate commodity exchange activities in the Republic of Kazakhstan.</p> <p>The regulatory authority is the Committee on Trade, part of the Ministry of Economic Development and Trade.</p> <p>Relevant legislation: the Civil Code of the Republic of Kazakhstan (based on the Civil Code for the CIS member states), law no. 155-IV “On Commodity Exchanges” (April 4, 2009) and a number of other laws, including more than 50 government resolutions and legislative acts.</p>

Country	State regulation of commodity exchange activities
Russian Federation	<p>The regulatory authority for the organised commodity market in the Russian Federation is the Federal Service for Financial Markets, which exercises statutory regulation, control and supervision of financial markets (but not banking and auditing activities). The Federal Service for Financial Markets was established in accordance with Presidential Decree no. 314 (of March 9, 2004), "On the System and Structure of the Federal Executive Authorities" and based on provisions adopted in Government Decree no. 717 (August 29, 2011) and RF Government Decree no. 326 (April 26, 2011) "On Issues Relating to the Activities of the Federal Executive Bodies in the Financial Market Sphere". The Federal Service for Financial Markets is controlled by the Government of the Russian Federation.</p> <p>Key legislation:</p> <p>The Civil Code (based on the model civil code for the CIS countries) and Federal Law no. 2383-I (February 20, 1992) "On Commodity Exchanges and Exchange Trading".</p> <p>Federal laws:</p> <ul style="list-style-type: none"> • no. 325-FL "On Organised Trading" (November 21, 2011); • no. 7-FL "On Clearing and Clearing Activities" (February 7, 2011); • no. 99-FL "On Licensing of Certain Types of Activity" (May 4, 2011); • no. 63-FL "On Electronic Signatures" (April 6, 2011). <p>Some secondary legislation.</p>
Republic of Belarus	<p>State regulation of commodity exchange activity is executed by the President, the Council of Ministers, the Ministry of Trade and other government bodies within their competence as defined by law. The Coordinating Committee on Commodity Market Trading was set up to facilitate interaction between state bodies and commodity exchanges on matters relating to commodity trading.</p> <p>Key legislation: The Civil Code (based on the model Civil Code for the CIS countries).</p> <p>Laws: "On Commodity Exchanges" (no. 10-Z of January 5, 2009), "On Trading" (no. 231-Z of July 28, 2003), "On Electronic Documents and Electronic Digital Signatures" (no. 113-Z of December 28, 2009).</p> <p>The main secondary act is the Resolution of the Council of Ministers of Belarus "On Measures for Implementing the Law on Commodity Exchanges" (no. 1039 of August 6, 2009), the provisions of which cover:</p> <ul style="list-style-type: none"> • the regulations governing trading on commodity exchanges, the procedures for setting up and using a commodity exchange guarantee fund and the composition of the Coordinating Committee on exchange trading. <p>Other secondary legislation.</p>
Ukraine	<p>In Ukraine, there is no single body responsible for regulating the organised commodity market. The National Commission on Securities and the Stock Market operates in accordance with the decree of the President of Ukraine "On the National Commission on Securities and the Stock Market" (no. 1063/2011 of November 23, 2011). The above law authorises the National Commission on Securities and the Stock Market to regulate the derivatives market.</p> <p>The organised grain market is regulated by Ukraine's Ministry of Agrarian Policy and Food Production, according to the Presidential Decree "On the Ministry of Agrarian Policy and Food Production" (no. 500/2011 of April 23, 2011).</p> <p>The Ministry of Energy and the Coal Industry is authorised by the Presidential decree "On Regulation of the Ministry of Energy and the Coal Industry" (no. 382/2011 of April 6, 2011) to implement an exchange market development programme.</p> <p>Key legislation: the Civil Code (not based on the CIS model Civil Code).</p> <p>Laws: "On Commodity Exchanges" (no. 1956-XII of December 10, 1991), "On Electronic Digital Signatures" (no. 852-IV of May 22, 2003) and the Resolution of the Cabinet of Ministers of Ukraine "On Intensification of the Exchange Market for Agricultural Products and the Material Resources Required" (no. 1928 of October 19, 1999).</p> <p>Other secondary legislation as adopted.</p>

Analysis of relevant legislation in the member states revealed that:

1. Belarus moved quickly to set up its commodity exchanges. Secondary legislation has been adopted to regulate many aspects of commodity exchange activity and a developed commodity exchange infrastructure already exists. Supply logistics and commodity exchange infrastructure, including warehousing facilities and foreign representation, are particularly well developed on the Belarus Universal Commodity Exchange (BUCE).
2. Russian legislation has been adapted to reflect developments in organised commodity markets. Changes include the strengthening of transaction guarantees, the regulation of forward contract trading and the clearing and settlement of forward contracts on stock and commodity markets.
3. Kazakh legislation on the regulation of organised commodity markets underwent important changes in 2009–2012. However, separate regulation of the derivatives market on stock and commodity exchanges has discouraged futures and options transactions. A uniform approach to the regulation of transactions on both markets, using financial instruments, may be required.
4. In Ukraine, there are discrepancies between the regulations on commodity market infrastructure and the legislation establishing the regulations.

The Ukrainian law “On Commodity Exchanges” (no. 1956 XII of December 10, 1991) is typical of regulatory legislation enacted in the 1990s, which treats the exchange market as though it were a spot market. Derivatives – like clearing – have only become subject to legislation relatively recently and they are only covered in relation to the stock market. Due to their structure, commodity markets should be regulated differently to stock markets. In Russia, this important distinction has been taken into account, although there has been a steady movement towards more general regulation in recent years.

In Russia and Ukraine, current regulation of organised commodity markets does not include international or transnational commodity exchange transactions. Adoption of the Russian Federal Law “On Organised Trading” (no. 325-FL of November 21, 2011) has brought changes, but comprehensive regulation can only be achieved by creating additional mechanisms.

Whilst the Ukrainian law “On Commodity Exchange” (no. 1956-XII of December 10, 1991) allows the participation of foreign physical and legal entities, the Russian law “On Commodity Exchanges and Exchange Trading” (no. 2383-I of February 20, 1992), whilst allowing foreign membership, restricts foreign participation in exchange transactions. Whatever requirements are put in place, foreign participants must be allowed to operate on the commodity exchange and have access to clearing and settlement services within the member state in which the organised trading takes place.

Authorities regulating the organised commodity markets and their powers

In accordance with the legislation of the member states of the SES+, organised commodity market regulation falls within the competence of the relevant authority of the individual member state. Individual member states have adopted very different approaches to the issue of market regulation.

State	Comment
Republic of Kazakhstan	The Trade Committee of the Ministry of Economic Development and Trade of the RK is the authorised body regulating the organised commodities market. This committee is authorised to regulate and supervise trading activity in accordance with the laws of the Republic of Kazakhstan.
Russian Federation	The authority regulating the organised commodities market is the Federal Service for Financial Markets. This body is responsible for the statutory regulation, control and supervision of financial markets (but not banking and auditing activities). This body also monitors and supervises insurance, credit cooperation and microfinance activities and commodity exchange operations and regulates commodity exchange intermediaries and brokering activities. It ensures compliance with Russian legislation adopted to combat the wrongful use of insider information and market manipulation.
Republic of Belarus	Commodity exchange regulation is implemented by the President, the Council of Ministers, the Ministry of Trade and other government bodies within their competence as defined by law. The Ministry of Trade is authorised to regulate the following: <ul style="list-style-type: none"> • compliance with commodity exchange legislation; • the drafting and submission to the Council of Ministers of proposals on improving commodity exchange legislation; • other activities, as provided for by legislation. The Coordinating Committee is an interagency body set up to facilitate interaction on trading matters between state bodies and commodity exchanges.
Ukraine	In Ukraine, there is no single body responsible for regulating the organised commodities market. The National Commission on Securities and the Stock Market is a state body accountable to the President and the Verkhovna Rada and authorised to regulate the securities market. According to its statutes, this commission is responsible for regulating the derivatives market, but in essence its main area of regulation is the stock market. Development of the derivatives market is included in a state programme for stock market development. The organised grain market is regulated by Ukraine's Ministry of Agrarian Policy and Food Production. The Ministry of Energy and the Coal Industry is authorised to implement a programme of development for the coal exchange market.

Barriers to the functioning of an organised commodities market, its participants and the goods traded

Each member states of the SES+ has adopted legislation for the purposes of regulating the organised commodity market. Legislation relates to **three groups**:

1. The organisers of commodity exchange trading and their activities
2. The participants in commodity exchange trading
3. The objects of commodity exchange trading

1. Restrictions on the organisers of commodity exchange trading and their activities:

Country	Restrictions
Republic of Kazakhstan	<p>Commodity exchanges, exchange brokers and dealers are licensed in accordance with the law "On Licensing" (no. 214-III of November 11, 2007).</p> <p>The commodity exchange is prohibited from carrying out any trading activity not directly connected with the organised commodities market.</p> <p>The commodity exchange may not be involved in setting the fees payable to brokers and dealers carrying out intermediary activities.</p> <p>Transactions may not be made on behalf of the commodity exchange.</p> <p>A commodity exchange may not have fewer than seven members. Legal entities affiliated to the commodity exchange are not allowed to be members of the commodity exchange.</p> <p>Commodity exchange staff may not carry out transactions or use commercial information in their own interests.</p> <p>State procurement must be carried out in double-auction mode and only by means of electronic exchange trading.</p>
Russian Federation	<p>Organised trading may only be transacted by holders of exchange or trading system licences.</p> <p>Trading organisers may not engage in trading and insurance activities, operate credit facilities, provide accounting services for the holders of securities, manage incorporated investment funds, mutual investment funds or private pension funds, become a depository for investment funds, mutual funds or non-state pension funds, or participate in incorporated investment funds or non-state pension funds relating to pension provision and pension insurance.</p> <p>Trading organisers may not carry out central counterparty activities.</p> <p>Organisations combining activities relating to the organisation of trade with other types of activity must be legally structured to ensure such activities are carried out separately.</p> <p>Organisations combining activities relating to the organisation of trade with other types of activity must take appropriate measures to prevent any conflict of interests.</p> <p>Commodity exchanges must have the legal commercial structures of a joint stock company. Commodity exchanges may not participate in brokering activities, may not act as dealers or depositories and may not undertake activities involving securities management.</p>
Republic of Belarus	<p>Commodity exchanges may only carry out activities associated with the organisation and regulation of exchange trading, unless permitted otherwise by law. Commodity exchanges may not participate in exchange trading or offer brokering services to clients.</p> <p>The founders (participants) of a commodity exchange, by virtue of their investment in charter capital, or in accordance with agreements made between them, or in accordance with other arrangements, shall be entitled to influence decisions made by the said commodity exchange. Commodity exchange founders are prohibited from engaging in exchange transactions carried out on their own exchange, may not use any commercial information relating to that exchange in their own interests and may not disclose confidential information on trading participants or the clients of exchange brokers, or any activities relating thereto.</p> <p>Commodity exchange employees may not participate in exchange transactions and may not work in the employment of (and/or conclude any civil legal contract with) an exchange trading participant. Commodity exchange staff may not use confidential information relating to trading participants, the clients of exchange brokers, or any activities relating thereto in their own interests, or disclose such information.</p>
Ukraine	<p>The following commodity exchange activity is prohibited:</p> <ul style="list-style-type: none"> • actions agreed between exchange trading participants and carried out with the intention of changing or fixing current exchange prices, or carried out in the knowledge that such actions are likely to lead to changes in current exchange prices; • the dissemination of false information likely to lead to an artificial change in market conditions; • the selling of exchange commodities (contracts), directly or through the agency of a nominee, with the intention of influencing price dynamics.

2. Some of the restrictions placed on commodity exchange participants in the member states of the SES+ are as follows:

State	Restrictions
Republic of Kazakhstan	<p>In accordance with the legislation of Kazakhstan, the activities of commodity exchange brokers and dealers shall be based on licences issued by the authorised body. Under current legislation, foreign brokers and dealers may not participate in exchange trading, since they are not legal entities registered in the Republic of Kazakhstan.</p> <p>Commodity exchanges shall be entitled to establish additional qualifying requirements for exchange membership, e.g., minimum charter capital, minimum period of market participation.</p> <p>Professional securities market participants may not carry out transactions on the commodity futures market in the absence of a central counterparty, as stated in Article 33 of the law "On the Securities Market".</p> <p>Exchange trading participants may not offer less than 15% of their own total commodity turnover under double-auction conditions (Article 4.2 of the law "On Commodity Exchanges").</p>
Russian Federation	<p>Individual traders and legal entities established in accordance with the laws of the Russian Federation, i.e., residents, shall be entitled to participate in organised trading (access to foreign legal entities is restricted).</p> <p>Foreign legal entities may be allowed to participate in organised trading if they are carrying out functions similar to those of an approved central counterparty. The foreign legal entity must appear on federal executive authority lists establishing restrictions on access to organised trading. In other words, foreign legal entities may only participate in organised trading as central counterparties.</p>
Republic of Belarus	<p>Only individual traders and legal entities registered in Belarus are entitled to operate as exchange brokers. Non-residents may not act as exchange brokers.</p> <p>No facility exists for the cross-accreditation of non-resident exchange brokers and such brokers may not therefore participate in trading on the floors of the commodity exchange of Belarus.</p> <p>Under the Resolution of the Council of Ministers of Belarus (no.1882 of December 5, 2008), producers and non-producers of selected products, including skimmed milk powder and industrial casein, shall be entitled to trade their export commodities under both exchange or off-exchange conditions.</p>
Ukraine	<p>State authorities and state-funded institutions (organisations) are not entitled to become commodity exchange founders or members.</p> <p>The law "On Commodity Exchanges" (no. 1956 – XII of December 10, 1991) restricts, but does not prohibit, the participation of foreign legal entities in commodity exchange transactions.</p>

3. Restrictions on exchange-traded goods established by the member states of the SES+:

State	Restrictions
Republic of Kazakhstan	<p>Temporary bans were introduced for six months from July 1, 2012 on the exportation of light distillates (Customs Union Commodity Classification of Foreign Economic Activity – FEACN CU (2710 12), kerosene (FEACN CU 2710 19 210 0 – 2710 19 250 0), gas oils (FEACN CU 2710 19 420 0 – 2710 19 480 0, 2710 20 110 0 – 2710 20 190 0) and other petroleum products (2710 20 900 0), except for special grades of gasoline (FEACN CU 2710 TS 12210 0 – 2710 12 250 0) and domestic heating oil.</p> <p>Commodities withdrawn from the market or with limited circulation, real estate and intellectual property may not be traded on the commodity exchanges.</p> <p>To support exchange trading, the government of the Republic of Kazakhstan has drawn up a list of commodities which may only be sold on commodity exchanges and has increased the minimum lot size (nine different commodities are currently listed).</p>
Russian Federation	<p>Commodities withdrawn from circulation may not be exchange traded.</p> <p>Mandatory requirements may be established in respect of commodity type and quality and commodities not meeting these statutory requirements may not be traded on exchange floors.</p> <p>Real estate or intellectual property may not be traded.</p> <p>Exchange trading – including long-term supply agreements – of a list of commodities approved by the government – is subject to mandatory registration by the commodity exchange. These commodities include the following:</p> <ul style="list-style-type: none"> • petroleum products, as permitted under supplementary regulations and sold by manufacturers included in the register of economic entities (excluding financial organisations) with commodity market share in excess of 35% or with a dominant position in the relevant product market and where federal law has established the dominant position of the said economic entity in respect of such markets; • crude oil, sold by manufacturers included in Paragraph 1 of the list referred to above; • coal, where sold by an economic entities under conditions of sale established by the entity and/ or by a group of entities to which that entity belongs, in the previous year and in volumes exceeding 1 million tonnes.
Republic of Belarus	<p>The establishment, in accordance with legislation, of minimum prices on certain exported goods, e.g., skimmed milk powder (FEACN CU 0402 10 190 0) at a minimum export price of €2500 per tonne and industrial casein (FEACN CU 3501 10 500 0) at a minimum export price of €6000 per tonne.</p> <p>The maximum and minimum prices for exchange commodities (the price corridor) are set at commodity exchange level. For example, the price corridor for skimmed milk powder, butter, cheese and industrial casein is set by the commodity exchange together with a working group set up by the Prime Minister of the Republic of Belarus to monitor sales of dairy products on domestic and foreign markets. The working group recommends the minimum prices on dairy products intended for export.</p>
Ukraine	<p>Certain commodities – including means of transportation and fixed assets – may only be exchange traded in lots.</p> <p>On the Ukraine grain market:</p> <ul style="list-style-type: none"> • restrictions are introduced on a regular basis, such as the mandatory registration of export contracts (on the Agrarian Exchange), quotas or emergency customs measures; • grain may only be traded on accredited exchanges. The accrediting bodies are the Ministry of Agriculture and the exchange itself. Grain may only be traded on the Agrarian Exchange.

Clearing and settlement procedures and conditions applied to those procedures

The legislation governing clearing and settlement procedures and regulating commodity exchange trading is different in each SES+ member state; commodity markets may or may not have the authority to settle export/import transactions in hard currency.

The regulations have been abridged for all the member states of the SES+ with the exception of Russia:

State	Restrictions on settlement and clearing
Republic of Kazakhstan	<p>According to the legislation of Kazakhstan, one of the functions of the commodity exchange is to organise payments in respect of exchange transactions. Commodity exchanges make all payments through banks or other institutions licensed to engage in banking operations. No licences are required for clearing operations carried out on commodity exchanges.</p> <p>According to its legal definition "clearing constitutes the offsetting of mutual claims and obligations between exchange trading participants in respect of transactions carried out on the commodity exchange".</p> <p>The agreement on exchange trading and transaction settlement procedures drafted by the commodity exchanges stipulates the conditions for participation of banks (or payment organisations), commodity exchanges and/or clearing houses in payment activities.</p> <p>For futures and option transactions, the commodity exchange organises payment through clearing centres.</p> <p>Clearing centres act as a central counterparty – as a buyer with respect to seller exchange transactions and as a seller with respect to buyer transactions. Clearing houses must have the commercial structure of a legal entity and be independent of the commodity exchange. Current legislation stipulates that exchange transactions may not be carried out on behalf of the commodity exchange.</p>
Russian Federation	<p>Clearing is defined as the enforcement of obligations arising from contracts, including those resulting from the carrying out of netting obligations, and the preparation of the documentation (information) on which the termination and/or enforcement of such obligations is based. Clearing services are a necessary condition of access to the concluding of transactions provided to participants by the trading organiser.</p> <p>Clearing is partially carried out centrally by clearing organisations.</p> <p>Clearing is carried out on the basis of documents provided by the trading organiser (not by the clearing participants) in respect of transactions concluded during trading.</p> <p>For futures and forward transactions, clearing is carried out separately for each participant trading account.</p>
Republic of Belarus	<p>The clearing of exchange transactions is carried out by the commodity exchange or by other organisations based on agreements made with the commodity exchange; payments resulting from clearing operations are made by the bank.</p> <p>There is no comprehensive set of procedures for the commodity exchange clearing of real goods. Only a range of clearing operations, such as the establishment of exchange deposit requirements, the accounting of free and leveraged deposits, the processing of documentation, confirmation of transaction execution, bank cooperation, etc., are carried out by the commodity exchange, based on local regulations.</p> <p>Settlement between exchange trading participants are carried out using one of the following:</p> <ul style="list-style-type: none"> • trading participants are permitted to make settlements using their accounts in different banks; • trading participants are obliged to use the bank accounts of the exchange <p>The Belarus Universal Commodities Exchange is not obliged to sell the foreign currency transferred into its account by trading participants and their clients, as a means of security against transaction obligation default.</p> <p>No licence is required to carry out these activities on the commodity futures market in the Republic of Belarus.</p>

State	Restrictions on settlement and clearing
Ukraine	<p>Clearing on organised commodity markets is not regulated by Ukrainian legislation. Clearing regulations appearing in Ukrainian legislation in 2012 relate primarily to the stock market.</p> <p>Payments in respect of exchange contracts, and the financial interventions or forward purchases carried out by the Agrarian Fund to secure their implementation, are made via the bank account of the Agrarian Exchange.</p> <p>Actual payment procedures are determined by the type of exchange contract.</p> <p>Payments made by the Agrarian Fund into the bank accounts of the Agrarian Exchange are normally conducted within one working day by written order of the General Director of the Fund.</p>

The following conclusions can be drawn from this summary of current regulation:

1. In all the SES+ countries, **with the exception of Russia**, no licence is required to carry out clearing activities in respect of transactions (including futures) carried out on commodity exchanges. Correspondingly, there are no charter capital requirements on clearing agencies, no qualification requirements for clearing agency staff and no information technology (programming software) requirements. Furthermore, there is no requirement for clearing centres to be separated from the commodity exchange structure.
2. Commodity exchange legislation **restricts the entitlement of commodity exchanges to participate in trading, conclude transactions in the name of the commodity exchange and carry out brokering activities**. This effectively means that there are no trading organisers in any of these countries able to organise forward trading without the help of external agencies or exchange institutions working in cooperation or under contract, since trading organisers have no entitlement to act as central counterparties in respect of such transactions. In the absence of any legislative requirements on such agencies, however, it is most unlikely that adequate levels of risk can be provided for participants in futures trading.
3. Russian legislation already prohibits trading organisers from acting in the capacity of central counterparties.
4. **The term “central counterparty” currently only appears in Russian and Kazakh legislation**; without such legislation, the development of trading on futures markets is virtually impossible.

Settlement of export/import exchange transactions and currency regulation

The settlement procedures in respect of export/import exchange transactions are carried out in accordance with national external trade legislation in each of the member states.

State	Commodity exchange participation in exchange transaction settlement
Republic of Kazakhstan	<p>Notwithstanding the provisions of Article 13 of the Law “On Commodity Exchanges” (no. 155-IV of May 4, 2009), which oblige commodity exchanges to organise exchange transaction settlements, commodity exchanges may not act as clearing and settlement organisations. Clearing may only be carried out by banks or other organisations engaged in banking activities. Clearing houses may only conclude agreements on exchange trading procedures and transaction settlements.</p>

State	Commodity exchange participation in exchange transaction settlement
Republic of Kazakhstan	<p>Depending on their internal trading and clearing regulations, commodity exchanges normally play only a minor role in export–import exchange transaction settlement. Settlement operations on export and import exchange transactions are normally carried out by currency transfers involving banks authorised in accordance with the currency legislation requirements of Kazakhstan. In accordance with international agreements, the Republic of Kazakhstan is legislating to liberalise foreign exchange, streamline foreign transaction procedures and accelerate the processing of transactions.</p>
Russian Federation	<p>In the Russian Federation, external trade and currency regulations are not linked with organised commodity market legislation.</p>
Republic of Belarus	<p>In Belarus, export and import exchange transaction settlement is conducted in accordance with legislation regulating external trade operations.</p> <p>This area of activity is governed by the Presidential Decree “On Procedures for Conducting and Controlling External Trade” (no. 178 of March 27, 2008), hereinafter referred to as the Decree). According to Sub–paragraph 1.4 of Paragraph 1 of the Decree, residents must complete their external trade transactions, as follows:</p> <ul style="list-style-type: none"> • export transactions – no later than 90 calendar days (or, for commission contracts, no later than 120 calendar days) from the date of shipment of the goods (transfer of protected information, exclusive rights to intellectual property), completion of the works or rendering of the services; • import transactions – no later than 60 calendar days from the date of payment. When importing, residents must ensure that goods are brought onto the territory of Belarus within the prescribed deadlines. <p>The date of completion of any external trade operation is taken to be the date on which the funds are transferred into the bank account of the commodity exchange.</p> <p>Currency operations must be carried out in accordance with legislation on currency regulation.</p> <p>Currency regulation and control is governed by the Law “On Currency Regulation and Currency Control” (no. 226–W of July 22, 2003).</p> <p>According to Paragraph 2 of Presidential Decree no. 577 of September 14, 2006, the Belarus Universal Commodities Exchange is exempt from the obligatory sale of 30% of all foreign currency transferred by exchange trading participants and their clients, as means of security against transaction obligation default.</p>
Ukraine	<p>Payments in respect of exchange contracts, and the financial interventions or forward purchases carried out by the Agrarian Fund to secure their implementation, are made via the bank accounts of the Agrarian Exchange. Actual payment procedures are determined by the type of exchange contract.</p> <p>Payments made by the Agrarian Fund into the bank accounts of the Agrarian Exchange are normally conducted within one working day by written order of the General Director of the Fund.</p> <p>The Cabinet of Ministers of Ukraine has decreed that the exportation of grain may only be carried out on the basis of transactions registered at the Agrarian Exchange.</p> <p>When drawing up foreign economic contracts with non–residents of Ukraine, the price of the transaction shall be stated in the relevant foreign currency. Transaction payments shall be made at the rates of exchange calculated by the National Bank of Ukraine on the day of trading.</p> <p>Contracts shall be drafted on the official forms issued by the Agrarian Exchange and a certificate of registration must be provided. The final page of the registration certificate must carry the registration number, date and signature of the exchange employee and the stamp and seal of the Agrarian Exchange.</p> <p>Separate registration procedures are in place for spot and forward contracts. A record is kept of all registered foreign economic contracts.</p>

The information in the above table indicates the following:

1. **In Russia and Kazakhstan, export trade and currency regulation is not linked with legislation relating to organised commodity markets.** Currency legislation in the Republic of Kazakhstan does not take into consideration the specific nature of transactions concluded on commodity exchanges. Commodity exchanges and clearing centres can therefore run into problems when making client settlements. Questions arise as to the convertibility of currencies obtained from non-residents and transferred to residents, since current legislation on currency regulation does not permit transfer without conversion.
2. **In Belarus and Ukraine, the option of using special commodity exchange accounts for such settlements is envisaged** and currency regulations contain provisions that take into account the specific details of such settlements. However, the regulation of these issues is state-specific and there are exemptions from the usual contract requirements and procedures when concluding export contracts on commodity exchanges. The relevant documentation is completed by brokers on behalf of their clients.

Forward markets in the context of an organised commodities market

The forward market is at a different stage of development in each of the member states of the SES+ studied. A revival in commodity markets began in 2008. In Russia, traders, brokers, major producers and commodity consumers came together to try and improve exchange market practices. Trading floors were created and new commodity instruments introduced. Many commodity exchanges became futures markets, with no contractual ties to the price of basic assets. This resulted in the alienation of real market participants and the process of establishing a futures market stalled.

Even so, gradually – and mostly thanks to the subsequent efforts of brokers, the commodity exchange and the banks – positive steps are being taken to create a futures market that attracts commodity exchange participants. In Russia, there is nascent interest in these markets, and liquidity and turnover are increasing.

Attempts have been made to develop a futures market on the Kazakh commodity exchange with state participation and capital – Eurasian Trading System PLC has even created interest on other exchanges.

In Belarus, trading in commodity futures began at the end of 2012 on the Belarus Universal Commodities Exchange. The emergence of a futures market on the BUCE is an important event for Belarus and will allow the country to work more actively with its CIS partners. The main problem encountered by the commodity exchange in organising a futures market was a lack of knowledge regarding the commercial entities active in this form of trading.

The forward market section of the Ukrainian commodity market was launched on May 27, 2010 with futures being traded on Index UX. Within a few months, this became the Ukrainian stock market's most liquid instrument. On April 26, 2011 – just one year later – a second trading instrument was launched – futures options on Index UX. There is no trading of forward contracts on the commodity market.

A summary of forward market conditions in the member states of the SES+ is given below.

State	Comment
Republic of Kazakhstan	<p>Forward trading on commodity exchanges in the Republic of Kazakhstan is defined as “the trading of contracts for the conditional/unconditional sale or purchase of basic assets with deferred execution”, which includes futures and options.</p> <p>Options are simply defined as “exchange transactions involving options”.</p> <p>Futures are defined as “exchange transactions involving the payment of a pledge, settlement of which is made via a clearing centre”. Futures are traded out using fixed-term contracts obliging participants to receive/deliver a given volume of goods at some future point in time at a price fixed at the moment of transaction.</p> <p>Under Article 128-2 of the Civil Code, options, futures, forwards, swaps and other derivative financial instruments are defined together as “a type of contract, the price of which is dependent on the value (changing value) of a given basic asset and the payment of which is set at some future date”. The basic assets underlying derivative financial instruments can be goods, standardised lots of goods, securities, currencies, indices, interest rates and other assets with a market value dependent upon future events or circumstances.</p>
Russian Federation	<p>Derivative financial instruments are defined as “contracts which can be concluded during exchange trading”. The basic assets underlying these contracts are exchange commodities. Forwards, futures and options are all types of derivative financial instruments.</p>
Republic of Belarus	<p>The forward market in Belarus is being created on the basis of a project developed by the SSI – the Centre for System Analysis and Strategic Studies of the National Academy of Sciences of Belarus. The forward market concept has been agreed by the National Bank, the Ministry of Economics, the Ministry of Finance, the Ministry of Trade and the Ministry of Taxation and has been approved by the First Deputy Prime Minister of Belarus.</p> <p>Futures are transactions by means of which rights and obligations are created and in the course of which standard contracts are concluded.</p> <p>Options are transactions involving the transfer of rights and obligations at some future date and performed in respect of exchange commodities using standard contracts.</p> <p>According to Article 19 of the law “On Commodity Exchanges” (no. 10-3 of January 5, 2009), the standard contracts concluded on commodity exchanges in respect of futures or option transactions are not classified as securities.</p>
Ukraine	<p>In accordance with the law “On Commodity Exchanges”, a commodity exchange transaction is an agreement which meets all of the following conditions:</p> <ol style="list-style-type: none"> an agreement involving the purchase, sale, supply or exchange of any commodity that can be traded on a commodity exchange; an agreement made between members of a commodity exchange; an agreement registered on a commodity exchange not later than one day following the date on which it is concluded. <p>No definition of futures is given in the law “On Commodity Exchanges”. Forward market legislation in Ukraine is primarily focused on the stock market. Article 194 of the Civil Code of Ukraine (VVRU, 2003: 356) gives the following definition:</p> <p>“A security is a document confirming the right to cash or property, which defines the relationship between the individual issuing the security and the individual receiving it, envisages fulfilment of all and any obligations appertaining to it and allows for the transfer of the given right to a third party.”</p>

This report of futures market regulation on the commodity exchanges of certain member states suggests the following:

1. Current legislation governing futures transactions carried out on the commodity exchanges of the SES+ member states differs from country to country:

- **In Russia, futures are regarded as transactions involving financial instruments –** a transition to more unified regulation is under way which means that futures will be

regarded as transactions concluded under organised trading conditions on commodity and/or financial markets, with requirements on organisers and participants determined in accordance with the state regulation and control of the given activity.

- **In Kazakhstan, futures are understood as derivative financial instruments traded on organised commodity markets.** Legislation distinguishes between the securities market and the commodity exchange market. The essential difference between these two markets is a complicating factor in the development of a futures market on the commodity exchange market.
- In Belarus, futures traded on the commodity exchange are not regarded as securities.
- In Ukraine, it is unlikely that futures will be regarded as transactions carried out on the commodity exchange. They are more likely to be viewed as securities, as defined in the Ukrainian Civil Code. This means that the legislation affecting the futures market will be the same as that used to regulate the stock market.

2. The development of futures markets on the organised commodity markets of the SES+ member states will require important legislative changes to be made in each country.

State support for the development of an organised commodity market and cooperation between state authorities

State support for the development of organised commodity markets in the member states of the SES+ is being offered under widely differing conditions, reflecting the different stages of development each country has reached. In Russia and Kazakhstan, efforts are being made to develop competition on the organised commodity market.

In Russia, according to data published on the official website of the Federal Service for Financial Markets, there were 13 exchanges on the Russian Commodity Market on October 26, 2012 licensed to organise trading and 386 organisations with licences to act as exchange intermediaries, carrying out commodity futures and options transactions in commodity market trading.

In Kazakhstan, according to the Trade Committee of the Ministry of Economic Development and Trade a total of 18 commodity exchanges and 445 commodity brokers and dealers were in operation on September 1, 2012.

In Belarus, state regulation is focused on developing the BUCE, which is given special status on the commodity market. The BUCE has a total of 88 accredited brokers.

In Ukraine, as the foundations of an organised commodities market are being developed, work is under way to encourage a grain market and establish the legal status of the agricultural commodities exchange. There are more than 500 registered commodity exchanges in Ukraine.

Belarus, therefore, has only one commodity exchange and government legislation is formulated according to its needs. In Russia, legislation favours unified regulation of the futures market on both the commodity and stock markets, as adopted under the federal laws "On Organised Trading" (no. 25-FL of November 21, 2011) and "On Clearing and Clearing Activity" (no. 7-FL of February 7, 2011). However, the nature of exchange commodity trading makes the development of an organised commodity market more complex, and a separate,

single regulator will be necessary in this area. If such a regulator is not provided, further development of the commodity market is likely to prove difficult.

In Kazakhstan, activity on organised commodity and securities markets is sanctioned by legislation and subject to state regulation, so futures and options fall into the legislative provision for both markets. Consequently, regulatory norms are not independent and clashes occur when they are applied. For example, licensing has been established for clearing activities carried out with financial instruments on the securities market, but no requirements exist for the same activities on the commodity market. In accordance with the Civil Code of the Republic of Kazakhstan and the law “On Commodity Exchanges” (no. 155–IV of May 4, 2009), commodity exchanges are entitled to trade futures and options, which are regarded as derivative financial instruments. In addition, legislation and regulation in respect of the securities market is more advanced than regulation of the organised commodities market. This is an obstacle to the normal relationship between these separate markets and is, in fact, one of the major stumbling blocks in the development of the futures and organised commodities market in Kazakhstan.

Regulation of the organised commodity market in Ukraine also suffers from being too fragmented. Divisions between economic sectors mean secondary legislation often falls under the jurisdiction of different economic departments.

Tax on commodity exchange transactions

In accordance with current legislation and international agreements ratified by the countries studied, commodity exchange transactions are liable for tax.

State	Comment
Republic of Kazakhstan	<p>The goods and commodities transferred in exchange transactions may be subject to tax on turnover and import tax. The turnover realised by entities paying value added tax (VAT) is taxable.</p> <p>The current rate of VAT is 12% and this tax is applicable to all taxable turnover and taxable imports.</p> <p>Turnover realised from export sales is taxable at the zero rate.</p>
Russian Federation	<p>Operations not subject to VAT (exempt from taxation) include futures transactions, but not futures transactions involving basic assets subject to VAT.</p> <p>When trading basic asset futures on organised markets (but not basic asset options contracts), the tax base is defined as the price at which the basic asset must be sold, as determined by the futures financial instrument conditions specified by the exchange. When selling basic assets, the tax base is defined as that specified in Article 167 of the Tax Code of the Russian Federation, inclusive of excise taxes (on excisable goods).</p> <p>The zero tax rate is applied to goods sold for export, as specified in customs procedures.</p> <p>A 10% tax is applied to sales of food products, including milk, milk products and grain.</p> <p>In all other cases (not specified in the tax legislation of the RF), taxation is applied at the rate of 18%.</p> <p>In accordance with tax legislation, petrol and diesel are liable for excise duty. The excise rates on these products are as follows:</p> <ul style="list-style-type: none"> • petrol (but not Classes 3, 4 and 5), from July 1, 2012 – 8225 roubles per tonne; from January 1, 2013 – 10,100 roubles per tonne; from January 1, 2014 until December 31, 2014 – 11,110 roubles per tonne. The excise rates on petrol in Classes 3, 4 and 5 are correspondingly lower. • diesel (but not Classes 3, 4 and 5): from July 1, 2012 – 4300 roubles per tonne; from January 1, 2013 – 5860 roubles per tonne; from January 1, 2014 until December 31, 2014 – 6446 roubles per tonne. The excise rates on diesel in Classes 3, 4 and 5 are correspondingly lower.

State	Comment
Republic of Belarus	<p>The taxation of exchange transactions is based on VAT and varies depending on type of exchange commodity and type of transaction (export, import, domestic market).</p> <p>The zero VAT rate is applied to exchange transactions involving exports.</p> <p>Import and/or the sale of food and children's products included in lists approved by the President of the Republic of Belarus (including milk, milk products and skimmed milk powder) are subject to 10% tax.</p> <p>Sales and imports of goods, other than those listed above are taxed at 20%.</p>
Ukraine	<p>Income generated by all operations is subject to a profits tax. Under current tax laws, the basic rate of tax is 16%.</p> <p>The VAT rate is 20% (from January 1, 2014 – 17%).</p>

The further development of international commodity exchange activity is obstructed by the difference in VAT rates (18% in Russia; 20% in Belarus; 12% in Kazakhstan) and excise duty on petrol and diesel in the different countries.

International agreements between Customs Union member states came into force on July 1, 2010 regulating VAT on imports and exports, works carried out and services rendered, and VAT administration on mutual trade. They include:

- agreement on the principles of exemption from indirect taxation on exports and imports and on works carried out and services rendered (January 25, 2008);
- protocol amending the agreement on the principles of exemption from indirect taxation on exports and imports and on works carried out and services rendered from January 25, 2008 (December 11, 2009);
- protocol on exemption from indirect taxation and on monitoring payment of taxes for exports and imports (December 11, 2009);
- protocol on indirect tax exemption procedures in respect of works carried out and services rendered (December 11, 2009);
- protocol on the exchange of electronic information between the tax authorities of the member states of the CU on the indirect tax paid (December 11, 2009).

Under the agreement on the principles of exemption from indirect taxation on exports and imports, works carried out and services rendered, exemption from indirect taxation (VAT and excise duty) on mutual trade between the member states of the CU shall be governed by the "country of destination" principle, according to which exports shall be subject to VAT at the zero rate and imports shall be subject to VAT at the rate in force in the country in which the importer is located.

The internal legislation and international agreements adopted by member states shall regulate all issues relating to the administration of indirect taxation and shall be aimed at eradicating all instances of incomplete payment in respect of indirect tax levied on goods imported onto the territories of the Republics of Kazakhstan, Belarus and the Russian Federation.

5.2. Analysis of member state legislation relating to electronic document distribution and the use of electronic digital signatures in cross-border transactions

The internal legislation of each SES+ member state contains special statutes regulating electronic document distribution, electronic digital signatures and the circumstances in which they may be used.

The main statutes and laws in this field are:

- Republic of Kazakhstan's law "On Electronic Documents and Electronic Digital Signatures" (no. 370-II of January 7, 2003);
- Republic of Belarus' law "On Electronic Documents and Electronic Digital Signatures" (no. 113-Z of December 28, 2009);
- Russian Federal law "On Electronic Signatures" (no. 63-FL of April 6, 2011);
- Ukraine's law "On Electronic Digital Signatures" (no. 852-IV of May 22, 2003), law "On Electronic Documents and Electronic Document Distribution" (of May 22, 2003),
- Republic of Uzbekistan's law "On Electronic Document Distribution" (no. 611-II of April 29, 2004), and law "On Electronic Digital Signatures" (no. 562-II of December 11, 2003);
- Republic of Moldova's law "On Electronic Documents and Digital Signatures" (no. 264-XV of July 15, 2004);

One potential issue affecting electronic documentation and electronic signatures for cross-border transactions is the use of foreign registration certificates (or other documents confirming the correspondence of electronic signatures for internal legislative requirements) and the conditions of acceptance of electronic signatures on the territories of other SES+ member states.

State	Comment
Republic of Kazakhstan	<p>Current legislation relates to foreign registration certificates and the exchange of electronic documents with foreign individuals and legal entities. Relations between the certifying centre and foreign registration certificate holders are governed by legislation on issuing registration certificates, unless the parties agree otherwise. No agreements on recognising foreign registration certificates between the Republic of Kazakhstan and the other SES+ countries have yet been ratified.</p> <p>Foreign digital signatures are only recognised in the Republic of Kazakhstan, where the relevant international treaty has been ratified or the foreign registration certificate has been registered. Registration is undertaken by the certifying centre.</p>
Russian Federation	<p>Electronic signatures are recognised in the Russian Federation, provided they have been created in accordance with the regulations established by the relevant foreign state and comply with international standards. Electronic signatures and electronic documents carrying electronic signatures may not be considered invalid solely on the grounds that key validation certificates have been issued in accordance with foreign legislative requirements.</p>
Republic of Belarus	<p>Foreign public key certificates complying with foreign legislation are recognised in the Republic of Belarus, in accordance with international agreements to which Belarus is signatory.</p> <p>Public key certificates issued by foreign service providers accredited by the state key management system are recognised in Belarus.</p>

State	Comment
Ukraine	Foreign key certificates, legitimised in accordance with the laws of the states where they are issued, are recognised in Ukraine. However, no regulatory procedures have been established in law.
Republic of Uzbekistan	Foreign electronic signature key certificates may be used, in accordance with the procedures established by Uzbek legislation.
Republic of Moldova	Public key certificates issued by foreign public key certification centres are recognised in the Republic of Moldova based on bilateral or multilateral agreements between Moldova and the relevant state or states, or (on a reciprocal basis) between Moldova and international organisations.

The CU member states have signed an agreement on the use of information technology to exchange electronic documents for internal and mutual trade within the single customs area (Moscow, September 21, 2010); the agreement also establishes the conditions for accepting electronic documents by CU member states. On Page 10 of the said agreement and in order to protect the interests of CU members and encourage the use of electronic document distribution for cross-border transactions, "... a trusted third party:

- shall legalise (confirm authenticity) of the electronic documents;
- shall provide security guarantees for the international (cross-border) exchange of the electronic documents;
- shall guarantee the legitimacy of using electronic digital signatures on incoming and/or outgoing messages and documents, in accordance with legislation of the member state in which the trusted third party is located."

Trusted third parties shall cooperate in establishing the security of electronic documents transferred between member states using different mechanisms to protect those documents.

The parties shall grant cooperating member states the right to use the services of trusted third parties, the functions of which shall be carried out by the state authorities of the cooperating states or by organisations accredited by the said state authorities.

An integrated information system for external and mutual trade in the Customs Union is to be implemented subject to agreement (Moscow, September 21, 2010). This cooperative project focuses on member state information systems and resources that regulate external and mutual trade. The project also relates to the information systems and the CU Commission resources responsible for integrating the systems of each CU member state.

The work is due to be completed by the end of 2013.

Electronic document distribution plays an important role in the customs administration of cross-border transactions involving exchange commodities. A project to improve customs administration within the CU in 2012–2015 is under way. The main issues for electronic document distribution are:

- 1) Introducing the principle of priority for electronic documents and information in electronic format, including the installation of customs technology and the drafting of legislation ("electronic" takes priority over paper); customs technology must be able to handle legally valid electronic document applications;

- 2) Providing effective, “quality” customs declarations in electronic format and using customs declarations for not less than 90–95% of the itemised goods and storage. Retaining written declarations for specific goods categories;
- 3) Introducing complex (score) evaluations into all supply chains (sender, receiver, transporter, contract holder, storage facility, broker, etc.).

In the international agreement drafted for SES+ member states on the acceptance of foreign electronic digital signatures, the principle established in Article 20 of the model law “On Electronic Digital Signatures” (adopted at the XVI plenum of the Interparliamentary Assembly of the CIS on December 9, 2000) should be adopted. This states that foreign electronic digital signatures can be accepted, provided they can be checked by public key and are supported by certification issued by one of the CIS member states signatory to the above agreement, or to any other agreement providing an equivalent level of electronic message security.

5.3. National systems for regulating clearing and activities involving transactions with basic commodity market assets

Russia’s federal law “On Clearing and Clearing Activities” (no. 7–FL of February 7, 2011) governs the execution of clearing, requirements for legal entities engaged in clearing and/or the functions of central counterparties, and the state regulation of clearing operations and state controls over their implementation. The key provisions relating to clearing in Russia, both on the securities and organised commodity markets are contained in this law, namely:

- definitions of clearing operations, clearing organisations, clearing participants, clearing regulations, central counterparties, organised trade, netting, commodity supply operators and others;
- statutory requirements for clearing organisations and persons acting as central counterparties; for controlling authorities and persons working in clearing organisation; for the founders of (and participants in) clearing organisations; for the proprietary funds of clearing organisations and other standard obligations (a minimum level of proprietary funding for clearing organisations of 100 billion roubles). The requirements for persons intending to engage in clearing are given in the clearing regulations referred to above;
- the law also governs the opening of trading and clearing accounts and establishes regulations governing trading and clearing–account operations. Clearing bank accounts may be opened either in roubles or in foreign currencies. Clearing–type commodity accounts may be opened by commodity supply operators, provided records of the said commodities are kept on the basis of storage agreements, as set out in Article 17 of the current federal law. Operations on the above accounts are treated as commodity transfers (or receipts);
- the above law embraces the best practices adopted by organised commodity markets, and also by the stock market, in that these regulation of both markets is brought together in this one law.

Clearing activities are regulated in the Republic of Kazakhstan as follows:

- clearing using financial instruments on the securities market was first licensed as a professional activity after laws “On the Securities Market” and “On Licensing” were amended in July 2012.
- clearing organisations must hold minimum proprietary funds of not less than 500,000 times the specified rate

Clearing using financial instruments on organised commodity markets is regulated by the law “On Commodity Exchanges”, which does not actually list any requirements in respect of clearing. The securities market regulator, therefore, actually blocks access to the commodity exchange futures market for professional brokers and dealers. This negatively affects the development of the futures market, since it makes it much harder to attract experienced securities market brokers and dealers and the financial resources to which they have access.

Clearing is restricted in Belarus and only individual clearing operations are possible: there are requirements on commodity exchange deposits, on the free and/or leveraged parts of such deposits, on documentation confirming transaction fulfilment, on mutual cooperation with banks, etc. The settlements resulting from clearing are executed by clearing banks.

5.4. National settlement and currency regulation systems for international transactions involving basic commodity exchange assets

At present, there is no Russian or Kazakh legislation on settlement norms or regulating currency settlements of international transactions involving basic commodity market assets traded on organised commodity exchanges. Laws relate to transactions on commodity markets as if they were national and therefore governed by domestic legislation. As a rule, such settlements are paid in the domestic currency. It should be noted that Ukrainian legislation, which covers a very wide spectrum of instances requiring the individual currency licences, restricts the participation of Ukrainian entities in international commodity exchange transactions.

A similar situation is envisaged in the legislation of the Republic of Belarus. Imports and exports of cash assets under external trade contracts concluded in respect of commodity market trading on the BUCE can be credited to its bank account in Belarus. The BUCE is legally entitled to open special accounts as under Article 1.3, Point 1 of the Presidential Decree “On Issues Relating to the Activity of Belarus Universal Commodity Exchange PLC (no. 577 of September 14, 2006). To guarantee security, the BUCE is not obliged to sell any foreign currency transferred to its accounts by exchange trading participants and/or the clients of such participants.

Kazakh legislation makes no special provision for the settlement of commodity exchange transactions.

5.5. Existing conditions supporting integration of an organised commodities market

The integration of the member states of the CIS and the SES is gathering momentum: the process of creating a single economic, financial and banking zone is under way and

supranational bodies are being created in various spheres. These processes are vital in increasing trade between the member states in the future and will support the creation of an organised commodities market.

The prerequisites for integration of the organised commodities market of the SES+ efforts are being established. International agreements on cooperation in various fields have been signed by the SES+ member states to encourage the setting up of an organised commodities market in these countries.

One such agreement is the Free Trade Zone (FTZ, St. Petersburg; October 18, 2011). This document sets out the priorities for full and effective operation of a free trade zone between the member states of the CIS and helps create the conditions needed for deeper integration in the future based on WTO standards. The agreement also provides a simplified legal framework for economic relations between the participant states and regulates free trade across the territories of the CIS.

Remove the various restrictions embodied in national legislation is seen as an important precondition for integrating the organised commodities market of the SES+ member states and this process – in Russia, Kazakhstan and Belarus, at least – is being actively pursued.

Similarities in the regulations established by national law:

- participation is already well regulated by individual laws, but where such regulation exists it is often incorporated into legislation at different levels;
- this makes it difficult to introduce any new and complex procedures into existing legislation and means that existing legislation must be reviewed;
- legislation relating to commodity exchanges and their activities in the SES+ member states is much less advanced than banking legislation, currency regulation and securities market legislation and has been drafted without taking into account the normal operation and development of organised commodity markets;
- unless member state governments adopt a clear strategy focusing specifically on the creation of an organised commodities market involving all countries, and unless they agree principles of cooperation and amend their own legislation, integration cannot progress.

The SES+ states faced similar issues with regard to securities and they are now actively addressing these issues with regard to depositary activity on stock markets.

The following issues need to be addressed to pave the way for international cooperation on organised commodity markets:

1. A model for state cooperation at interexchange level, reinforcing how such cooperation will be structured, needs to be incorporated into an international treaty, the terms of which must envisage the phased introduction of the necessary changes to the legislation of each of SES+ member state.
2. Internal legislation must be adopted to allow foreign legal entities to participate in organised trading on the commodity exchanges of the SES+ member states, and to set out the conditions for such participation. Participants in trade may need to use

the infrastructures of neighbouring countries for certain types of trading: Direct and forward markets (spot and futures instruments); registration of off-market transactions dependent on commodity nomenclature.

3. Discrepancies in procedures for settlement of import/export contracts and in clearing/settlement regulations for commodity market transactions need to be eliminated and key principles of currency regulation should be harmonised.
4. A mechanism for reciprocal acceptance of electronic digital signatures for market trading is needed, similar to systems that exist in developed countries. Legislation is needed to establish reciprocal norms.
5. The model law "On Organised Trading" must be adapted as a way of changing the internal legislation of the SES+ member states.
6. It would be appropriate at this stage to form a committee consisting of the heads of the national authorities responsible for regulating organised commodities markets and market trading.
7. The specific nature of these markets mean that it would be desirable to invite experienced commodity exchange specialists from each participating state, and representatives of the IAE CIS and the EDB countries, to form a model interstate commodities market for CIS countries. Member state legislation needs to be drafted to implement the model. International documentation relevant to the development of international organised commodities markets and consistent with the internal legislation of participant states needs to be made available. Changes need to be made to national legislation taking into account the individual circumstances of each of the member states.
8. IAE CIS resources should be deployed to develop the appropriate model laws, which would help unify the legislative structures of the CIS countries.

6. Main conclusions

1. The absence of regulations in the laws of Russia, Kazakhstan and Belarus relating to cooperative commodity market activity is a barrier to cooperation. There is a pressing need to adopt and define priorities for the development of an organised interstate commodity exchange. This requires more detailed analysis of the problems affecting international cooperation relating to commodity exchanges and a long-term strategy aimed at creating a competitive interstate commodity exchange.
2. Differences the way commodity exchanges and trading activity are regulated constitute a serious stumbling block to commodity exchange interaction.
3. Legal barriers to the participation of foreign legal entities and individuals in commodity market trading are incorporated in the national legislation of the majority of the countries surveyed. In countries where changes have been envisaged, they cannot be implemented owing to contradictory provisions in secondary legislation.
4. Differences exist in the settlement procedures relating to import/export contracts. Currency regulation and clearing/settlement procedures for commodity exchange transactions differ in each of the participating countries.
5. There is no mechanism for reciprocal acceptance of electronic digital signatures in market trading activities at state level, even where national legislation allows for this.
6. Each of the participating countries has made significant efforts to safeguard the fulfilment of transaction obligations by counterparties and to develop infrastructure and commodity supply logistics. However, regulation of international cooperation on commodity market activity requires a unified approach.
7. Legislation that regulates commodity markets lags well behind regulation of the stock market and the banking sector. This situation needs to be improved, taking into account the specific nature of organised commodity markets.

The comparative analysis of the regulation of organised commodity markets in CIS countries should be used to develop a comprehensive model for a general commodities market in the CIS and SES member countries. This model should be based on general principles of operation and regulation with regard to professional participation, the requirements on trading organisers and commodity market assets, information transparency, the enforcement of transaction obligations and general risk management.

Many issues need to be addressed before the required level of legislative unification between the member states can be achieved. This will require the concerted efforts of regulators, trade organisers, the IAE CIS and other interested parties. A special authority dedicated to the sector needs to be created to regulate organised commodity markets and commodity trading, analogous to the work being done in respect of the stock markets in the CIS and EurAsEC countries.

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