

UNITED STATES OF AMERICA
Before the
COMMODITY FUTURES TRADING COMMISSION

RECEIVED
C.F.T.C.

OFFICE OF PROCEEDINGS
PROCEEDINGS CLERK

_____)
In the Matter of:)
)
ENSERCO ENERGY, INC.)
)
Respondent.)
)
)
)
)
_____)

CFTC Docket No. 03-222

**ORDER INSTITUTING
PROCEEDINGS PURSUANT TO
SECTIONS 6(c) AND 6(d) OF THE
COMMODITY EXCHANGE ACT,
MAKING FINDINGS AND
IMPOSING REMEDIAL SANCTIONS**

I.

The Commodity Futures Trading Commission ("Commission") has reason to believe that Enserco Energy, Inc. ("Enserco" or "Respondent"), a subsidiary of Black Hills Corporation ("Black Hills"), has violated Sections 6(c), 6(d) and 9(a)(2) of the Commodity Exchange Act, as amended (the "Act"), 7 U.S.C. §§ 9, 13b, 13(a)(2), and 15 (2001). Therefore, the Commission deems it appropriate and in the public interest that public administrative proceedings be, and hereby are, instituted to determine whether Enserco engaged in the violations set forth herein, and to determine whether any order should be issued imposing remedial sanctions.

II.

In anticipation of the institution of an administrative proceeding, the Respondent has submitted an Offer of Settlement (the "Offer"), which the Commission has determined to accept. Without admitting or denying the findings of fact herein, the Respondent consents to the entry of this Order in full and final settlement of any alleged violations of the above referenced laws or regulations solely as they relate to the activities and conduct described in Section C below, and acknowledges service of this Order Instituting Proceedings Pursuant to Sections 6(c) and 6(d) of the Commodity Exchange Act, Making Findings and Imposing Remedial Sanctions ("Order"). Respondent consents to the use by the Commission of the findings herein in this proceeding and in any other proceeding brought by the Commission or to which the Commission is a party.¹

¹ Respondent does not consent to the use of its Offer or the findings in this Order as the sole basis for any other proceeding brought by the Commission, other than a proceeding brought to enforce the terms of this Order. Respondent does not consent to the use of the Offer or the findings in this Order by any other person or entity in this or any other proceeding. The findings made in this Order are not binding on any other person or entity, including, but not limited to, any person or entity named as a defendant or respondent in any other proceeding.

III.

A. SUMMARY

From at least May 2000 through at least June 2002 (the "Relevant Period"), Enserco reported false information, including price and volume information, concerning natural gas cash transactions to certain reporting firms. Price and volume information is used by reporting firms in calculating published indexes of natural gas prices for various pipeline hubs throughout the United States. During the relevant period, Enserco knowingly reported trades that did not occur, reported certain actual trades at false prices and/or volumes, and did not disclose other actual trades, in an attempt to benefit the Respondent's trading positions.

B. RESPONDENT

Enserco Energy, Inc. is a South Dakota corporation with headquarters in Golden, Colorado and an office in Calgary, Alberta. During all times relevant hereto, Enserco engaged in natural gas marketing in the Rocky Mountain and West Coast regions of the United States. Enserco employed three full-time traders during the Relevant Period. Enserco is a wholly-owned subsidiary of Black Hills Energy, Inc., which in turn is a wholly owned subsidiary of Black Hills Corporation,² a publicly traded corporation listed on the New York Stock Exchange.

C. COOPERATION

Upon the recommendation of the Division of Enforcement ("DOE"), the Commission afforded substantial weight to Enserco's extraordinary level of cooperation in its decision to accept the Respondent's Offer. In less than three months, Enserco swiftly and aggressively investigated its trade reporting activities and provided DOE with detailed reports of its analyses and findings, as well as transcriptions of over one hundred relevant telephone recordings, and all other details related to its internal investigation, without asserting claims of attorney-client privilege or attorney-work product or requiring a limited waiver agreement. The Commission also took into consideration the small size of Enserco's trading operation and how it addressed the misconduct discussed in this Order. The Commission's determination to impose sanctions lower than it otherwise would have was based on the following considerations:

² Black Hills Corporation is a South Dakota Corporation with headquarters at 625 Ninth Street, Rapid City, South Dakota. The company's primary business activities are segregated into three operating groups: (1) a non-regulated integrated energy group, that, in addition to the natural gas marketing operations of Enserco, engages in oil and natural gas exploration and production, as well as independent power activities involving operation of a small group of non-regulated power plants; (2) a regulated electric utility that serves approximately 60,000 customers in South Dakota, Wyoming, and Montana; and (3) a communications group that provides broadband communications services to residential and business customers in western South Dakota.

1. In response to DOE's inquiry, Respondent promptly uncovered the nature and extent of the misconduct and brought it to the attention of DOE;
2. Respondent promptly disclosed the existence of the misconduct to the public;
3. Respondent committed to learning the truth expeditiously and simultaneously provided timely information and evidence to DOE, thereby reducing the government's investigation costs;
4. Respondent promptly produced a thorough and probing written report detailing the findings of its review. The evidence provided by Respondent was sufficient to facilitate prompt enforcement action;
5. Respondent and its parent company, Black Hills, employed the services of a major outside consulting firm to ensure that the company had proper risk controls. The consulting firm prepared a report of recommended changes that the company implemented;
6. There is no evidence that Black Hills had knowledge of, or participated in, the misconduct;
7. The persons responsible for Respondent's misconduct no longer work for Respondent;
8. Of his own volition, the President of Black Hills promptly and personally met with DOE staff to discuss and thoroughly review Respondent's misconduct; and
9. Respondent adopted, and the President of Black Hills assured DOE of, new and more effective internal controls and procedures designed to prevent a recurrence of the misconduct.

D. FACTS

1. Gas Market Participants' Use of Information from Reporting Firms

During the Relevant Period, reporting firms compiled and published indexes of natural gas prices for natural gas hubs throughout the United States. The indexes were calculated based upon trading information, including volume and price information, collected by the reporting firms from market participants. Participants in the natural gas markets use these indexes to price and settle commodity transactions. Moreover, natural gas futures traders refer to the prices published by the reporting firms for price discovery and for assessing price risks. For instance, an increase in prices at a natural gas trading hub signals either stronger demand or weakened supply and futures traders take account

of both price movements and changes in the supply/demand balance when conducting their futures trading.

2. Enserco Reported False Market Information

From at least May 2000 through at least June 2002, Respondent routinely delivered false reports to the reporting firms. These reports, submitted telephonically, contained nonexistent trades, as well as certain actual trades in which the price and/or volume was altered. Respondent on occasion also represented that its reports included all of its trades, when in fact certain actual trades were omitted.

The three Enserco traders delivered false trade information to reporting firms as part of a concerted and coordinated effort to benefit the Respondent's trading positions. Two of these traders were located in Enserco's Colorado office while the third was located in Canada. The traders attempted to capitalize on the fact that at least one reporting firm accepted reports from both offices for the same delivery points, unaware that the traders were employees of the same company.

The traders routinely made separate false reports to a reporting firm to increase significantly the likelihood that they could affect the published prices. They coordinated their reports in view of their existing positions, as exemplified by the following taped telephone conversation:

Trader A: Okay. Let's fire away at Sumas.
Trader B: So we want – you didn't buy enough [index based transaction], so you want it high; right?
Trader A: That's correct. That's correct. So I'm going to go 19 –
Trader B: 19 and a half is my mid. I'm going a high of 20 bucks too.
Trader A: Okay
Trader B: And SoCal we want low.
Trader A: Yeah.

E. LEGAL DISCUSSION

1. By Reporting False Market Information, Enserco Violated Section 9(a)(2) of the Act

Section 9(a)(2) of the Act makes it unlawful for any person “knowingly to deliver or cause to be delivered for transmission through the mails or interstate commerce by telegraph, telephone, wireless, or other means of communication false or misleading or knowingly inaccurate reports concerning crop or market information or conditions that affect or tend to affect the price of any commodity in interstate commerce[.]” *See, e.g., United Egg Producers v. Bauer Int'l Corp.*, 311 F. Supp. 1375, 1383 (S.D.N.Y. 1970) (concluding that false press releases regarding egg importation “tended to affect the price of eggs in interstate commerce”); *In re Soybean Futures Litig.*, 892 F. Supp. 1025, 1046

(N.D. Ill. 1995) (concluding that false reports can influence prices and constitute part of a manipulation claim).

Respondent violated Section 9(a)(2) of the Act when its employees knowingly delivered false price and volume information to the reporting firms.³ As discussed above, price and volume information affect or tend to affect the market price of natural gas, including futures prices as traded on the NYMEX. As such, Respondent violated Section 9(a)(2) of the Act.

2. By Attempting to Manipulate Prices, Enserco Violated Sections 6(c), 6(d) and 9(a)(2) of the Act

Sections 6(c) and 6(d) of the Act together authorize the Commission to serve a complaint and provide for the imposition of, among other things, civil monetary penalties and cease and desist orders if the Commission “has reason to believe that any person ... has manipulated or attempted to manipulate the market price of any commodity, in interstate commerce, or for future delivery on or subject to the rules of any registered entity ... or otherwise is violating or has violated any of the provisions of [the] Act.” Section 9(a)(2) provides that it is unlawful for “[a]ny person to manipulate or attempt to manipulate the price of any commodity in interstate commerce, or for future delivery on or subject to the rules of any registered entity, or to corner or attempt to corner any such commodity.”

The following elements generally are required to show an attempted manipulation: (1) an intent to affect the market price; and (2) some overt act in furtherance of that intent. *In re Hohenberg Bros. Co.*, [1975-1977 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 20,271 at 21,477 (CFTC Feb. 18, 1977). To prove the intent element of manipulation or attempted manipulation, it must be shown that Enserco “acted (or failed to act) with the purpose or conscious object of causing or effecting a price or price trend in the market that did not reflect the legitimate forces of supply and demand.” *In re Indiana Farm Bureau Cooperative Association*, [1982-1984 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 21,796 at 27,283 (CFTC Dec. 17, 1982). “[I]ntent is the essence of manipulation.” *Id.* at 27,282.

Respondent specifically intended to, and did, report false, misleading or knowingly inaccurate market information concerning trade prices and volume of trading in an attempt to manipulate the price of natural gas in interstate commerce. These actions constitute overt acts in furtherance of the attempted manipulation. By so doing, Respondent’s conduct constitutes an attempted manipulation under Section 9(a)(2) of the

³ Under Section 2(a)(1)(B) of the Act and Section 1.2 of the Commission’s Regulations, the act, omission, or failure of any official, agent, or other person acting for any individual, association, partnership, corporation, or trust within the scope of his employment or office shall be deemed the act, omission, or failure of such individual, association, partnership, corporation, or trust. “[I]t does not matter if the principal participated in or even knew about the agent’s acts; he is strictly liable for them.” *Stotler and Co. v. CFTC*, 855 F. 2d 1288, 1292 (7th Cir. 1988) (citing *Cange v. Stotler*, 826 F. 2d 581, 589(7th Cir. 1987); *Rosenthal & Co. v. CFTC*, 802 F. 2d 963, 966-67 (7th Cir. 1986)). Consequently, Enserco is liable for its employees’ violations of the Act.

Act, which, if successful, could have affected prices of NYMEX natural gas futures contracts.

IV.

FINDINGS OF VIOLATIONS

Based on the foregoing, the Commission finds that Respondent violated Sections 6(c), 6(d) and 9(a)(2) of the Act, 7 U.S.C. §§ 9, 13b, 13(a)(2) and 15 (2001).

V.

OFFER OF SETTLEMENT

Respondent has submitted an Offer of Settlement in which, without admitting or denying the findings herein, it acknowledges service of the Order; admits jurisdiction of the Commission with respect to the matters set forth in this Order and for any action or proceeding brought or authorized by the Commission based upon violations of or for enforcement of the Order; waives service and filing of a complaint and notice of hearing, a hearing, all post-hearing procedures, judicial review by any court, any objection to the staff's participation in the Commission's consideration of the Offer, any claim of double jeopardy based on the institution of this proceeding or the entry of any order imposing a civil monetary penalty or other relief, and all claims which it may possess under the Equal Access to Justice Act, 5 U.S.C. § 504 (1994) and 28 U.S.C. § 2412 (1996), as amended by Pub. L. No. 104-21, §§ 231-32, 110 Stat. 862-63 (1996), and Part 148 of the Commission's Regulations, 17 C.F.R. §§ 148.1 *et seq.* (2002), relating to, or arising from, this action; stipulates that the record basis on which this Order is entered consists solely of this Order, including the findings in this Order; and consents to the Commission's issuance of this Order. Pursuant to the Offer of Settlement herein, Enserco agrees to entry of an Order, in which the Commission makes findings, including findings that Enserco violated Sections 6(c), 6(d), and 9(a)(2) of the Act, and orders Enserco to: cease and desist from violating the provisions of the Act it has been found to have violated; pay a civil monetary penalty of three million dollars (\$3,000,000); and comply with the conditions and undertakings as set forth in this Order.

VI.

Accordingly, IT IS HEREBY ORDERED THAT:

1. Enserco shall cease and desist from violating Sections 6(c), 6(d), and 9(a)(2) of the Act.

2. Enserco shall pay a civil monetary penalty of Three Million Dollars (\$3,000,000) within ten business days of the date of the entry of this Order, and make such payment by electronic funds transfer to the account of the Commission at the United States Treasury or by certified check or bank cashier's check made payable to the

Commodity Futures Trading Commission and addressed to Dennese Posey, Division of Enforcement, Commodity Futures Trading Commission, 1155 21st Street, N.W., Washington, D.C. 20581, under cover of a letter that identifies the Respondent and the name and docket number of this proceeding. Copies of the cover letter and the form of payment shall be simultaneously transmitted to Gregory George Mocek, Director, Division of Enforcement, Commodity Futures Trading Commission, 1155 21st Street, N.W., Washington, D.C. 20581. If payment is not made in accordance with the requirements of this paragraph, Respondent shall be subject to further proceedings pursuant to Section 6(c) and Section 6(e)(2) of the Act, 7 U.S.C. § 9 and 9a(e)(2) (2001), for violating a Commission Order.

3. Respondent shall comply with the following conditions and undertakings as specified:

(a) **Future Cooperation With the Commission**

Respondent shall continue to cooperate fully and expeditiously with the Commission and its staff, including DOE, in this proceeding, and in any investigation, civil litigation, or administrative matter related to the subject matter of this proceeding or any current or future Commission investigation related thereto. Respondent agrees to cooperate fully and expeditiously with the Commission's ongoing efforts to discover documents and information related to reporting trade prices and/or volumes to energy reporting services and price indexes. As part of such cooperation, Respondent agrees to:

(1) preserve all records relating to the subject matter of this proceeding, including but not limited to audio files, e-mails, and trading records; and

(2) comply fully, promptly, and truthfully to any inquires or requests for information including but not limited to:

- (i) requests for authentication of documents;
- (ii) requests for any documents within Respondent's possession, custody, or control, including inspection and copying of documents;
- (iii) requests to produce any current (as of the time of the request) officer, director, employee, or agent of Respondent, regardless of the employee's location and at such location that minimizes Commission travel resources, to provide assistance at any trial, proceeding, or Commission investigation related to the subject matter of this proceeding, including but not limited to, requests for testimony, depositions, and/or interviews, and to encourage them to testify completely and truthfully in any such proceeding, trial, or investigation; and

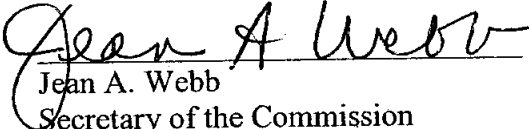
- (iv) requests for assistance in locating and contacting any prior (as of the time of the request) officer, director, or employee of Respondent.

Respondent also agrees that it will not undertake any act that would limit its ability to fully cooperate with the Commission. Respondent designates Geoffrey F. Aronow, Esq., of the Arnold and Porter law firm, to receive all requests for information pursuant to this undertaking. Should Respondent seek to change the designated person to receive such requests, notice shall be given in writing to the DOE of such intention 14 days before it occurs. Any person designated to receive such request shall be located in the United States.

(b) Public Statements

By neither admitting nor denying the findings of fact, Respondent agrees that neither it nor any of the agents or employees under its authority and control shall take any action or make any public statement denying, directly or indirectly, any findings or conclusions in the Order or creating, or tending to create, the impression that the Order is without factual or legal basis; provided, however, that nothing in this provision shall affect Respondent's: (i) testimonial obligations; or (ii) right to take factual or legal positions in other proceedings to which the Commission is not a party. Respondent will undertake all steps necessary to assure that all of the agents and employees under its authority and control understand and comply with this agreement.

By the Commission.


Jean A. Webb
Secretary of the Commission
Commodity Futures Trading Commission

Dated: July 31, 2003