

CFTC Letter No. 02-44**April 9, 2002****No-action****Division of Trading and Markets**

Re: Section 4m(1) of the Act -- Request for CTA Registration No-Action Position for the Operator of a Website that Automatically Generates Recommendations Regarding OTC Energy-Related Financial Instruments

Dear:

This is in response to your letter dated February 13, 2002, to the Division of Trading and Markets (the "Division") of the Commodity Futures Trading Commission (the "Commission"), as supplemented by telephone conversations with Division staff. By your correspondence, you request confirmation on behalf of "X" and its subsidiaries ("X") that the Division will not recommend that the Commission commence any enforcement action against "X" based solely upon "X's" failure to register under Section 4m(1) of the Commodity Exchange Act (the "Act")^[1] as a commodity trading advisor ("CTA") in connection with operating a web-based, interactive software system to assist bulk commercial users of natural gas and electricity in their risk management activities, including the users' trading decisions with respect to energy-related over-the-counter ("OTC") financial products.

Based upon the representations contained in your correspondence, we understand the facts to be as follows.

"X"

"X" is an affiliate of "Y" and it operates as part of the global "V" network in North America. The "V" network is an informal association of several companies of the "Z" group that trade in various commodities. "X" provides certain core services to midstream commercial, non-residential users of natural gas and electricity (those with an electric capacity of more than 5 megawatts or gas usage of more than 200 dekatherms per day). These services include physical supply and transportation of electricity and gas, energy risk management (in the sense of acting as consultant or as agent for benchmarking and tracking energy usage, managing utility projects to produce energy cost savings, and optimization of energy supplies), financing of energy supply and risk management, emissions credit trading, weather derivatives activity, and marketing and trading of power plant fuels and associated OTC derivatives activities. "X" does not engage in exchange-traded derivatives transactions on behalf of its customers, or advise its customers concerning such transactions. "X" does not have discretionary transactional authority over its customers' accounts and all risk management transactions result from arms-length negotiations with customers. Neither "X" nor any of its employees has sought registration as a CTA in connection with these activities.

“X” Website.

At the present time, “X’s” Internet website offers to persons who register on the site (who agree to posted “terms of use”) a range of energy price information from various exchanges, selected energy market news items and information links, weather updates, analytical and charting tools, and a selection of case studies, learning tools, white papers and reference materials. There is no fee charged, and the registered user can edit the screen to display the items the user finds most useful.

The Fundamental Forecasting Model.

In the near future, “X” plans to begin providing an additional level of services at its website involving scenario analyses produced by a fundamental forecasting model developed by “X” (the “FF Model”). The FF Model generates suggestions, based upon a number of inputs, for various types of OTC financial products^[2] offered by “X”.^[3] “X” will select the inputs (including whether the customer is a producer or consumer, the customer’s risk tolerance, weather forecasts and other assumptions and inputs) for each scenario it publishes on the website. The type of OTC products suggested by the FF Model will vary depending upon the inputs provided by “X”. “X” will use the FF Model to generate a representative sampling of scenario results, based on inputs selected and provided solely by “X”. These scenarios will change only as “X” periodically updates them with new data or assumptions. In this form, the FF Model will offer only generic advice not tailored to particular customers.

Please be aware that over-the-counter transactions such as those suggested by the FF Model in response to the scenarios composed by “X” may be entered into only by ECPs.

The Interactive Fundamental Forecasting Model.

In the future, “X” desires to make the FF Model interactive by permitting a subset of its registered website users to select and submit their own inputs. The interactive FF Model (the “IFF Model”) will process the customer-selected variables and generate suggestions regarding various types of energy-related OTC financial products.

The subset of visitors to “X’s” website to which the IFF Model would be offered consists of those who qualify as “eligible contract participants” (“ECPs”) as defined in Section 1a(12) of the Commodity Exchange Act (the “Act”).^[4] A user of the “X” website who registered and certified that the user was an ECP would be issued a separate password that would be required in order to gain access to the IFF Model. The general public and other users of the “X” website would not have access to the IFF Model.

“X” believes that the IFF Model will be more useful for “X” customers because it will permit them to develop scenarios geared specifically to their particular situations and needs, without reviewing scenarios that do not address their situations and needs. Customers using the IFF Model will be advised, however, that the suggestions offered refer only to privately-negotiated transactions between the

customer and “X”, or between the customer and another ECP. If “X” concludes that the IFF Model is providing a value-added service to its commercial customers, it may consider charging a monthly access fee to users of the IFF Model.

Analysis

In support of your request, you call to the Division’s attention Staff Letter 01-64,^[5] in which the Division found eligible for the exemption from CTA registration provided by Rule 4.14(a)(9) a website that provided non-personalized recommendations regarding purchasing, selling or hedging natural gas for bulk consumers and producers. The interactive aspect of the system described in Staff Letter 01-64 was restricted to a calculator function meant to enable a customer to compute the number and frequency of transactions required to carry out the system’s recommendation in the context of the customer’s volume production or consumption capacity. The recommendation remained unchanged and non-personalized. Unlike the situation in Staff Letter 01-64, the input of customer variables in the IFF Model determines the nature of the suggestion the model generates, and not just the number of contracts and transaction schedule. In this respect, Staff Letter 01-64 is not analogous to the facts you present.

Nevertheless, the fact that the suggestions that the IFF Model generates exclusively involve OTC, energy-related financial products, to be purchased and sold in privately-negotiated transactions, appears to place “X” outside the scope of any registration requirements of either the Act or the Commission’s rules. Pursuant to the Act, as amended by the Commodity Futures Modernization Act of 2000, energy-related financial products generally fall within the definition of “exempt commodity,”^[6] and transactions between ECPs involving those products that are not entered into on a trading facility are generally exempt from any provisions of the Act except antifraud and anti-manipulation prohibitions. Moreover, as you note, swap transactions that are privately negotiated between ECPs and not executed or traded on a trading facility are exempt from most provisions of the Act.

Conclusion

Based upon the representations made in your correspondence, it appears that “X” is not required to register as a CTA. This letter is based upon the representations made to us. Any different, changed or omitted facts or circumstances might require us to reach a different conclusion. Furthermore, this letter represents the views of this Division only and does not necessarily represent the views of the Commission or of any other office or division of the Commission.

This letter does not excuse “X” from compliance with any other applicable requirements contained in the Act or in the Commission’s rules thereunder. For example, “X” remains subject to the antifraud provisions of Sections 4b and 4o of the Act^[7] and rules thereunder, and to the reporting requirements for traders set forth in Parts 15, 18 and 19 of the Commission’s rules.

In addition, you are reminded that the OTC financial products suggested by the (non-interactive) FF

Model are available only to ECPs. Accordingly, “X” should take reasonable steps to make this fact clear to those who visit its website at the level of the FF Model (understanding, of course, that only ECPs will have access to the IFF Model).

If you have any questions concerning this correspondence, please contact me or Christopher W. Cummings, an attorney on my staff, at (202) 418-5445.

Very truly yours,

John C. Lawton
Acting Director

^[1] 7 U.S.C. §6m(1) (2000).

^[2] All of the products will be energy-related and none will be exchange-traded futures or options.

^[3] None of the suggestions generated by the FF Model will include any price information.

^[4] 7 U.S.C. §1a(12) (2000).

^[5] [2001-2002 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶28,577 (June 14, 2001).

^[6] See Sections 1a(14) and 2(h).

^[7] 7 U.S.C. § 6b and 6c (1994).