



U.S. COMMODITY FUTURES TRADING COMMISSION

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Division of Clearing and
Intermediary Oversight

James L. Carley
Director

CFTC letter No. 04-12
April 2, 2004
No-Action
Division of Clearing and Intermediary Oversight

Re: Request for No-Action Relief on Behalf of "X"

Dear :

This is in response to your letter dated January 28, 2004 to the Division of Clearing and Intermediary Oversight ("Division") of the Commodity Futures Trading Commission ("Commission") on behalf of your client, ("Company"), as supplemented by additional correspondence¹ and telephone conversations with Division staff.² By your letter, you request written assurance in the form of a no-action letter that the Division will not recommend any enforcement action against the Company for failure to register as a commodity trading advisor ("CTA") under the Commodity Exchange Act ("Act") based on the similarities between the Company and the energy management firm that was granted no-action relief from CTA registration in Staff Letter No. 02-59.³

Facts

Based upon representations made in the aforementioned correspondence and conversations, as well as the Company's website,⁴ we understand the facts to be as follows:

The Company is a privately held "Y" corporation that currently has 27 employee-owners. The Company's shareholders' agreement requires that all stockholders be active employees of the Company. Formed in 1992, the Company provides energy management, consulting, and engineering services.

¹ The Division received information by e-mail dated February 11, 2004.

² Division staff had discussions with you prior to the submission of your January 28, 2004 letter.

³ See CFTC Staff Letter No. 02-59, [2002–2003 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 29,063 (May 17, 2002).

⁴ See Company (visited February 3, 2004).

The Company engages in the management of energy services for natural gas and electricity end-users. The Company provides a number of energy management and invoicing services intended to reduce the energy costs of its customers and increase energy reliability. In this regard, the Company offers a full range of services, including price risk management, monthly billing reporting, review, verification and payment of monthly invoices, tariff review, contract negotiation, and procurement of electric and gas supply for customers who have multiple supplier options. The Company integrates the areas of invoice analysis, procurement, and usage management to produce a comprehensive energy management plan.

The Company may provide energy execution services upon a client's request, conducting purchases and sales in the forward and futures markets as agent for its customers. Any such transactions will be conducted pursuant to a power-of-attorney that gives the Company authority to make such trading decisions on the customer's behalf. The Company will not take title to any electricity it purchases on a customer's behalf, and it may engage in limited principal trades in the forward gas markets.

Although the Company intends to primarily make power purchases and sales in the forward markets, it also may establish hedge positions in the energy futures markets for its customers if market conditions and pricing so warrant. Futures or options trades for customers are executed based on the customer's underlying energy needs. The Company immediately reports to the customer each trade made on its behalf. The Company does not hold customer funds to support any commodity interest orders placed on behalf of a customer. The customer is expected to transfer any required funds to its futures commission merchant.

The Company does not offer trading services independent of its other services. Any trading of cash or futures instruments is directly linked to the overall strategic recommendations made by the Company which, in turn, are derived from the customers' energy needs. The Company is not a stand-alone trading advisor; it does not advertise or market its commodity trading services separately from the other services it performs, nor does it hold itself out as an expert in speculative trading. Specifically, the commodity trading services of the Company are only one product in a basket of products being offered, all intended to stabilize and hedge the price of gas or electricity for the customer.

The Company and its customers execute a Management Agreement that governs the contractual relationship between the parties. Under this contractual arrangement, the Company receives a fixed monthly fee, plus travel expenses.

The Company primarily markets its services to industrial and governmental customers.⁵ Each of its customers is or would qualify as an "eligible contract participant" as defined under Section 1a(12) of the Act. The Company will verify each customer's status as an eligible contract participant based on financial and other information that customers are required to

⁵ The Company's customer base is comprised of industrial customers (71 %), utilities (17%), and commercial customers (12%).

provide to the Company. In addition, customers will provide a specific representation to this effect in the Management Agreement that they enter into with the Company.

The Company does not, and does not plan to, provide or market its services to any commodity pool, passive collective investment vehicle, or any other entity not involved in natural gas or electricity consumption. The Company does not act as an agent for the purchase and sale of power in the wholesale energy market, nor does it own any generation or transmission facilities.

Statutory and Regulatory Background

In your no-action request, you state that by developing hedging strategies tailored to the needs of its customers, as well as engaging in purchases and sales involving swaps, forwards, or exchange-traded futures or options contracts on behalf of such customers for a fee, the Company will be deemed to be providing commodity interest trading advice to its customers for compensation or profit. You conclude that, consequently, the Company falls within the statutory definition of a CTA,⁶ with the resulting obligation to register under Section 4m(1) of the Act⁷ and Rule 4.14(a)(1) of the Commission's regulations.⁸ You have not asserted that the Company is exempt from registration under either Section 4m(1) of the Act or Rule 4.14(a)(1).

Discussion

You have represented that the Company is in a position substantially similar to that of the energy management firm that was granted relief in Staff Letter No. 02-59, except that the Company is not subject to regulation by the Federal Energy Regulatory Commission ("FERC"). Related to this, you have further represented that there is no FERC registration requirement applicable to the Company given that the Company does not take title to any electricity.

In view of all of the facts and circumstances presented, the Division believes that it is appropriate to take a no-action position with respect to the Company's failure to register as a

⁶ Section 1a(6) of the Act, 7 U.S.C. § 1a(6), defines a CTA generally as any person who, for compensation or profit, engages in the business of providing advice to others about the value or advisability of trading or using commodity futures or option contracts.

⁷ 7 U.S.C. § 6m(1). Section 4m(1) of the Act generally requires each person that comes within the CTA definition to register as such with the Commission. It exempts from registration any CTA who, during the course of the preceding twelve months, has not furnished commodity trading advice to more than 15 persons and who does not hold himself out generally to the public as a CTA.

⁸ 17 C.F.R. § 4.14(a)(1). This rule provides an exemption from registration for a CTA that is "a dealer, processor, broker, or seller in cash market transactions of any commodity (or product thereof) and the person's commodity trading advice is solely incidental to the conduct of its cash market business."

CTA. This no-action position is based upon, in particular, the increased use of market-based pricing in newly deregulated wholesale and retail electricity markets, the corresponding increase in the need for risk management strategies to hedge cash market transactions, and the representation that the Company's exchange-traded futures and options activities will be limited to hedging transactions on behalf of entities that would qualify as eligible contract participants. The Division believes that the absence of FERC regulation does not warrant denial of your request for no-action relief. In addition, the Division notes that the Company has represented that that none of the principals of the Company or any persons providing commodity trading advice to customers are subject to any of the statutory disqualifications from registration listed in Section 8a(2) of the Act, 7 U.S.C. § 12a(2).

Accordingly, the Division will not recommend that the Commission commence any enforcement action against the Company based solely upon the Company's failure to register as a CTA under Section 4m(1) of the Act in connection with providing commodity trading advice to its customers, as described above.

Other Matters

This letter is applicable to the Company solely in connection with its provision of energy management services to customers qualifying as eligible contract participants, as described above. It does not excuse the Company from compliance with any other applicable requirements contained in the Act or in the Commission's regulations issued thereunder. For example, the Company remains subject to all of the antifraud provisions of the Act and the Commission's regulations, to the reporting requirements for traders set forth in Parts 15, 18 and 19 of the Commission's regulations to the extent applicable, and to all otherwise applicable provisions of Part 4 of the Commission's regulations.

This letter and the no-action position taken herein are based upon the representations made by the Company. Any different, changed, or omitted material facts or circumstances might render this letter void. You must notify us immediately in the event that the operations or activities of the Company, including the range of services offered or the type of customer served, change in any material way from those represented to the Division. Moreover, this letter represents the position of the Division only and does not necessarily represent the views of the Commission or those of any other division or office of the Commission.

If you have any questions concerning this correspondence, please contact Phyllis Dietz, an attorney on my staff, at (202) 418-5430.

Very truly yours,

James L. Carley
Director