

# Clients & Friends Memo

## Unregistered CTA Summit Energy Services: Choose Your Words Wisely

February 9, 2015

A recent case highlights the importance of periodically reviewing an energy company's marketing materials and related activities (including statements made on websites) to ensure that the company is not holding itself out -- without CFTC registration -- as a CTA (commodity trading advisor). A number of exclusions and exemptions may apply to such activity, including exemptions for providing advice to fewer than 15 persons and for advice that is solely incidental to a cash market business. However, these exemptions are narrowly construed and governed by older no-action relief rather than the rule itself.

Market participants need to be mindful of the possibility of triggering CTA status and need to monitor whether employees are providing advice regarding CFTC-jurisdictional products, even in connection with the sale of physical energy or commodities to customers.

### What is a CTA?

The CFTC regulates persons and companies that, for compensation or profit, provide advice or guide the trading of another person with respect to CFTC-jurisdictional products (*i.e.*, futures, options on futures, swaps and options other than trade options). Such persons are deemed to be CTAs and are required to register with the CFTC unless they qualify for an exclusion or exemption. One such exemption from registration is for persons who provide commodity trading advice to fewer than fifteen persons within a twelve month period and do not hold themselves out generally to the public as CTAs. As mentioned above these exemptions are often narrowly construed. Additionally, the CFTC interprets the phrase "for compensation or profit" in the CTA definition very broadly. If you are providing commodity trading advice and don't qualify for an exemption or exclusion, you have likely triggered the CTA registration requirements even if there is no readily apparent compensation or profit involved.

### The Summit Energy Case

On January 16, 2015, the CFTC entered an order requiring Summit Energy Services Inc. to pay a civil monetary penalty in the amount of \$140,000 for acting as a CTA without having registered as

such. The CFTC's order stated that Summit Energy was, for compensation or profit, engaging in the business of advising more than fifteen clients as to the value of or the advisability of trading in natural gas swaps and natural gas commodity futures contracts.

### Summit Energy's CTA Activity

Summit Energy provides energy management and sustainability services to organizations in a wide range of industries to help control energy cost and mitigate risk for its clients. According to the CFTC's findings, during the relevant (approximately) two year period most of Summit Energy's clients were commercial entities that purchase physical natural gas and electricity and it provided those clients with advice regarding such physical transactions. Providing advice regarding physical transactions alone, however, does not generally trigger CTA registration requirements. Instead, Summit Energy (who was not registered with the CFTC in any capacity at the time)<sup>1</sup> also provided its clients with advice as to the value of or the advisability of trading in natural gas OTC swaps and futures for hedging purposes.<sup>2</sup> Further, the CFTC determined that Summit Energy was holding itself out to the public as a CTA by "offering to others its risk management services, including commodity trading advice concerning natural gas futures and OTC swaps, through its website and sales brochures."

The CTA registration requirements were triggered because the advice was provided to more than 15 clients, and no other exemption or exclusion applied (the CFTC also noted that Summit Energy's commodity trading advice was not solely incidental to its business). The CFTC determined that Summit Energy was acting as an unregistered CTA and had violated Section 4m(1) of the CEA. Accordingly, Summit was required to pay a \$140,000 civil monetary penalty and cease and desist from acting as an unregistered CTA.

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Please feel free to contact any of the following Cadwalader lawyers if you have any questions about this Clients & Friends Memo.

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<sup>1</sup> In September 2014 Summit Energy became a registered CTA.

<sup>2</sup> The CFTC noted that with respect to some of its clients, Summit Energy also acted as a broker in OTC natural gas swaps. It is not clear what role this fact played in the CFTC's analysis.