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COMMODITY FUTURES TRADING COMMISSION

17 CFR Part 37

RIN 3038-AE25

Swap Execution Facilities

AGENCY: Commodity Futures Trading Commission.

ACTION: Final rule.

SUMMARY: The Commodity Futures Trading Commission ("Commission" or "CFTC") is adopting final rules ("Final Rules") addressing operational issues facing swap execution facilities ("SEF") and their market participants in connection with the Commission's regulatory requirements for a SEF's audit trail data, financial resources, and chief compliance officer ("CCO").

DATES: This rule is effective [INSERT DATE 90 DAYS AFTER DATE OF PUBLICATION IN THE *FEDERAL REGISTER*].

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I. Background and Introduction

A. Statutory and Regulatory History

Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act")[1] amended the Commodity Exchange Act ("CEA" or "Act")[2] to establish a comprehensive new swaps regulatory framework that includes the registration

[1] *See* Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111-203, title VII, 124 Stat. 1376 (2010) (codified as amended in various sections of 7 U.S.C.), *https://www.cftc.gov/sites/default/files/idc/groups/public/@lrfederalregister/documents/file/2013-12242a.pdf.*

[2] 7 U.S.C. 1 *et seq*.

and oversight of SEFs.[3] As amended, CEA section 1a(50) defines a SEF as a trading system or platform that allows multiple participants to execute or trade swaps with multiple participants through any means of interstate commerce.[4] CEA section 5h(a)(1) requires an entity to register as a SEF prior to operating a facility for the trading or processing of swaps.[5] CEA section 5h(f) requires registered SEFs to comply with fifteen core principles.[6] Further, CEA section 2(h)(8) provides that swap transactions subject to the clearing requirement in CEA section 2(h)(1)(A)[7] must be executed on a designated contract market ("DCM"), SEF, or a SEF that is exempt from registration pursuant to CEA section 5h(g),[8] unless (i) no DCM or SEF[9] "makes the swap available to trade" or

[3] 7 U.S.C. 7b-3 (adding CEA section 5h to establish a registration requirement and regulatory regime for SEFs).

[4] 7 U.S.C. 1a(50).

[5] CEA section 5h(a)(1) states that no person may operate a facility for the trading or processing of swaps unless the facility is registered as a SEF or as a DCM under section 5h. 7 U.S.C. 7b-3(a)(1).

[6] 7 U.S.C. 7b-3(f). From herein, the term "SEFs" refers to registered SEFs, unless otherwise indicated.

[7] Section 723(a)(3) of the Dodd-Frank Act added a CEA section 2(h) to establish the clearing requirement for swaps. 7 U.S.C. 2(h). CEA section 2(h)(1)(A) provides that it is unlawful for any person to engage in a swap unless that person submits such swap for clearing to a derivatives clearing organization that is registered under the CEA or a derivatives clearing organization that is exempt from registration under the CEA if the swap is required to be cleared. 7 U.S.C. 2(h)(1)(A). CEA section 2(h)(2) specifies the process for the Commission to review and determine whether a swap, group, category, type, or class of swap should be subject to the clearing requirement. 7 U.S.C. 2(h)(2). The Commission further implemented the clearing determination process under part 50, which also specifies the swaps currently subject to the requirement. 17 CFR part 50.

[8] CEA section 2(h)(8)(A)(ii) contains a typographical error that specifies CEA section 5h(f), rather than CEA section 5h(g), as the provision that allows the Commission to exempt a SEF from registration. Where appropriate, this reference is corrected in the discussion herein.

[9] CEA section 2(h)(8)(A)(i)-(ii) provides, with respect to transactions involving swaps subject to the clearing requirement that counterparties shall execute the transaction on a board of trade designated as a contract market under section 5; or execute the transaction on a swap execution facility registered under section 5h or a swap execution facility that is exempt from registration under section 5h(g) of the CEA. Given this reference in CEA section 2(h)(8)(A)(ii), the Commission accordingly interprets "swap execution facility" in CEA section 2(h)(8)(B) to include a swap execution facility that is exempt from registration pursuant to CEA section 5h(g).

(ii) the transaction is subject to a clearing requirement exception pursuant to CEA section 2(h)(7).[10]

Pursuant to its discretionary rulemaking authority in CEA sections 5h(f)(1) and 8a(5), the Commission identified the relevant areas in which the statutory SEF framework would benefit from additional rules or regulations.[11] Accordingly, in 2013, the Commission adopted part 37 of its regulations to implement a regulatory framework for SEFs and for the trading and execution of swaps on such facilities ("2013 SEF Rules").[12]

Subsequently, a number of SEFs and their market participants requested relief from certain part 37 requirements they found in practice to be operationally unworkable or unnecessarily burdensome. A number of SEFs indicated that some of those requirements are impractical or unachievable due to technology limitations, or are incompatible with existing market practices. For example, as discussed further below, a number of SEFs stated that the requirement to include post-execution allocation information in audit trail data under § 37.205 is operationally difficult and impractical to implement.[13] Even where SEFs were able to comply with certain requirements, they asserted that (i) the compliance costs are high, and (ii) compliance is unnecessary to satisfy their self-regulatory obligations and the statutory SEF core principles. For

[10] 7 U.S.C. 2(h)(8). This is referred to as the "trade execution requirement."

[11] To implement the SEF core principles, Core Principle 1 provides that the Commission may, in its discretion, determine by rule or regulation the manner in which SEFs comply with the core principles. 7 U.S.C. 7b-3(f)(1)(B).

[12] Core Principles and Other Requirements for Swap Execution Facilities, 78 FR 33476 (Jun. 4, 2013) ("SEF Core Principles Final Rule"); Process for a Designated Contract Market or Swap Execution Facility to Make a Swap Available to Trade, Swap Transaction Compliance and Implementation Schedule, and Trade Execution Requirement Under the Commodity Exchange Act, 78 FR 33606 (Jun. 4, 2013).

[13] 17 CFR 37.205; *see* Section II, *infra*.

instance, SEFs noted that the financial resources requirements imposed by Core Principle 13 regulations are capital-intensive and broader than the specific costs of compliance with SEF regulatory obligations.[14] In response to concerns regarding the financial resources requirement and other requirements operationally difficult and impractical to implement, Commission staff issued a combination of no-action relief and guidance in the months and years following the adoption of part 37.[15]

In November 2018, the Commission issued a notice of proposed rulemaking under CEA sections 5h(f)(1) and 8a(5), seeking to address these issues by codifying relevant staff no-action relief or otherwise resolving the concerns of SEFs and market participants.[16] The proposed rules ("Proposed Rules") also set forth structural reforms to the SEF regime beyond these operational fixes. In particular, the Proposed Rules would have removed existing limitations on swap execution methods,[17] while expanding both

[14] *See* Comment Letter from Wholesale Markets Brokers' Association, Americas ("WMBAA"), Swap Execution Facility Regulations, Made Available to Trade Determinations, and Swap Trading Requirements at 5 (Mar. 11, 2016), *http://www.wmbaa.com/wp-content/uploads/2016/06/WMBAA_Letter_to_CFTC_031116.pdf.*

[15] *See, e.g.*, CFTC Staff Letter No. 17-54, Re: No-Action Relief for Swap Execution Facilities from Certain Audit Trail Requirements in Commission Regulation 37.205 Related to Post-Execution Allocation Information at 2 (Oct. 31, 2017) ("CFTC Staff Letter No. 17-54"); CFTC Staff Letter No. 15-26, Division of Market Oversight Guidance on Calculating Projected Operating Costs by Swap Execution Facilities (Apr. 23, 2015) ("CFTC Staff Letter No. 15-26"); and CFTC Staff Letter No. 17-25, Division of Market Oversight Guidance on Calculating Projected Operating Costs By Designated Contract Markets and Swap Execution Facilities (Apr. 28, 2017) ("CFTC Staff Letter No. 17-25"); CFTC Staff Letter No. 17-61, Re: No-Action Relief for Swap Execution Facilities from Compliance with the Timing Requirements of Commission Regulation 37.1501(f)(2) Relating to Chief Compliance Officer Annual Compliance Reports and Commission Regulation 37.1306(d) Relating to Fourth Quarter Financial Reports at 2-3 (Nov. 20, 2017) ("CFTC Staff Letter No. 17-61").

[16] Swap Execution Facilities and Trade Execution Requirement, 83 FR 61946 (Nov. 30, 2018).

[17] Under § 37.9(a), any transaction involving a swap subject to the trade execution requirement in section 2(h)(8) of the Act ("Required Transactions") must be executed in accordance with (i) an Order Book as defined in § 37.3(a)(3); or (ii) a request for quote ("RFQ") to no fewer than three market participants in conjunction with an Order Book. 17 CFR 37.9(a). Transactions not subject to the trade execution requirement ("Permitted Transactions") may trade via any execution method.

the categories of swaps that must be executed on a SEF, and the types of entities that must register as SEFs. Commenters to the Proposed Rules uniformly favored adopting certain of the narrower operational proposals.[18] By contrast, the Proposed Rules' broader market reforms elicited a number of comments expressing hesitation regarding the expansive scope of the proposed changes and recommending the Commission instead focus on more targeted improvements to the existing swap trading regulatory regime.[19]

Accordingly, the Final Rules implement certain operationally-focused proposals that received limited and generally positive feedback from commenters—namely, targeted changes to requirements for a SEF's audit trail data, financial resources, CCO governance, and timing of CCO reports.

B. Summary of Final Rules

In summary, the Final Rules make the following changes to the SEF regulatory regime:

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[18] *See, e.g.*, Comment Letter from Bloomberg at A-6 (Mar. 15, 2019) (expressing support for proposed changes to financial resources liquidity requirement) ("Bloomberg Letter"); Comment Letter from Refinitiv at 11, 13-14 (Mar. 13, 2019) ("Refinitiv Letter") (expressing support for proposed changes to financial resources and audit trail requirements); Comment Letter from WMBAA (Mar. 15, 2019) ("2019 WMBAA Letter") (expressing support for proposed changes to financial resources, audit trail, and CCO requirements).

[19] *See, e.g.*, Comment Letter from the Alternative Investment Management Association at 1-2 (Feb. 25, 2019) (urging the CFTC "to approach any change to swap execution facilities and trade execution in a phased and targeted manner, rather than adopt a wholesale package of changes in a single rulemaking"); Comment Letter from Managed Funds Association at 2-3 (Mar. 15, 2019) (expressing concern with the breadth of the Proposed Rules and recommending targeted rather than comprehensive changes to the swap trading framework); Comment Letter from IATP at 3-4 (Mar. 15, 2019) (same); Comment Letter from Securities Industry and Financial Markets Association at 1 (Mar. 15, 2019) ("SIFMA Letter") (same); Comment Letter from SIFMA Asset Management Group at 1 (Mar. 15, 2019) (same); Comment Letter from Tradeweb Markets LLC at 1-2 (Mar. 14, 2019) (same); Comment Letter from Wellington Management Company LLP at 1 (Mar. 15, 2019). *See also* Comment Letter from Futures Industry Association at 7-9 (Mar. 15, 2019) (stating proposed market reforms "would present tall operational challenges and impose substantial costs on all market participants"); Comment Letter from Commodity Markets Council at 2 (Mar. 15, 2019) (same).

(1) *Audit trail data*. The Final Rules eliminate the requirement of a SEF to capture and retain post-execution allocation information in its audit trail data.

(2) *Financial resources*. The Final Rules apply the existing Core Principle 13 financial resources requirements to SEF operations in a less burdensome manner, including through amendments to the existing six-month liquidity requirement and the addition of new acceptable practices providing further guidelines to SEFs for making a reasonable calculation of their projected operating costs.

(3) *CCO*. The Final Rules streamline requirements for the CCO position, allow SEF management to exercise greater discretion in CCO oversight, and simplify the preparation and submission of the required annual compliance report ("ACR").

II. Audit Trail Requirements Related to Post-Execution Allocation Information

A. Background and Proposed Rules

Existing § 37.205(a) requires a SEF to capture and retain all audit trail data necessary to detect, investigate, and prevent customer and market abuses.[20] This audit trail data must permit a SEF to track a customer order from the time of receipt through fill, allocation, or other disposition.[21] Commission regulation 37.205(b)(2)(iv) requires a SEF's audit trail program to include an electronic transaction history database that identifies, among other things, each account to which order fills are allocated.[22]

During the SEF registration process starting fall 2013 through spring 2016, numerous SEFs indicated that post-execution allocations are made away from SEFs and

[20] 17 CFR 37.205(a). Such audit trail data must be sufficient to reconstruct all indications of interest, RFQs, orders, and trades.

[21] *Id.*

[22] 17 CFR 37.205(b)(2)(iv).

typically occur between the clearing firm or the customer and the derivatives clearing organization ("DCO") or at the middleware provider.[23] Those SEFs represented they typically do not have access to post-execution allocation information and are unable to obtain this data from third parties, such as DCOs and swap data repositories, due to confidentiality concerns. Based on these representations, Commission staff issued no-action relief from this requirement.[24]

Recognizing the practical difficulties SEFs face in obtaining information regarding allocations occurring away from the SEF after a trade has been executed, the Commission proposed to eliminate the requirements in § 37.205(a) and (b)(2) that a SEF capture post-execution allocation information in its audit trail.[25] Instead, the Proposed Rules only require a SEF to capture and retain in its audit trail information through the execution of a trade on the SEF.[26] The Commission noted that this change would be consistent with current swap market practices.[27]

B. Summary of Comments

Commenters support the proposal to eliminate the requirement to capture and retain post-execution allocation information.[28] According to Refinitiv and WMBAA,

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[23] CFTC Staff Letter No. 15-68, Re: No-Action Relief for Swap Execution Facilities from Certain Audit Trail Requirements in Commission Regulation 37.205 Related to Post-Execution Allocation Information (Dec. 22, 2015). at 2. As stated therein, "[e]ven if SEFs could obtain the information from DCOs, swap data repositories, or middleware providers, or alternatively, from the counterparties to the swap, the infrastructure necessary to securely transmit the post-execution allocation information, such as an application-programming interface or secure file transfer protocol site, is currently not in place."

[24] *Id.*; CFTC Staff Letter No. 17-54.

[25] 83 FR at 62005.

[26] *Id.*

[27] *Id.*

[28] Refinitiv Letter at 11 ("Refinitiv SEF supports the elimination of the requirement to be able to track an order through fill, allocation or other disposition, because SEFs generally do not have access to most post-

SEFs remain unable to obtain post-execution allocation information.[29] WMBAA believes "SEFs cannot and should not be responsible for collecting trade allocation information when the allocations occur away from the SEF" and the proposed changes "more accurately reflect the capabilities of SEFs to capture audit trail data."[30] In WMBAA's view, the proposed changes to SEF audit trail requirements "will [not] lead to degradation of the ability to reconstruct a trade and the environment in which it is traded."[31]

C. Final Rules

The Commission has determined, based on representations from SEFs, that SEFs are unable to obtain post-execution allocation information and is adopting the amendments to § 37.205(a) and (b)(2) as proposed. Moreover, the Commission is able to obtain post-execution allocation information from other registered entities and market participants, and is not aware that SEFs' reliance on the relief from collecting and retaining post-execution allocation has raised any regulatory concerns.

As commenters noted, post-execution allocation generally takes place between the clearing firm or the customer and the DCO, or at the middleware provider. DCOs are required to maintain records of all information necessary to record allocation of bunched orders for cleared swaps.[32] In addition, under § 1.35 managers of accounts eligible for post-execution allocation must maintain records sufficient to permit the reconstruction of

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execution information."); 2019 WMBAA Letter at 12-13 ("The WMBAA supports the Commission's proposal regarding audit trail requirements.").

[29] Refinitiv Letter at 11; 2019 WMBAA Letter at 12.

[30] 2019 WMBAA Letter at 12.

[31] *Id.* at 12-13.

[32] 17 CFR 39.20(a)(2).

the handling of the order from the time of placement by the account manager to the allocation to individual accounts, and introducing brokers, futures commission merchants, and SEF members must similarly maintain records of each order subject to post-execution allocation and the accounts to which the orders are allocated.[33] These required records must be made available to the Commission upon request.[34] Accordingly, the Commission expects that it will continue to have access to post-execution allocation information from these registered entities and market participants even after SEFs are no longer required to capture this information.

III. Financial Resources Requirements

A. Background and Overview of Proposed Rules

Core Principle 13 requires a SEF to have adequate financial, operational, and managerial resources to discharge each of its responsibilities.[35] To achieve financial resource adequacy, a SEF must maintain financial resources sufficient to cover its operating costs for a period of at least one year, calculated on a rolling basis.[36] The Commission implemented Core Principle 13 by adopting §§ 37.1301 through 37.1307 to specify (i) the eligible types of financial resources that may be counted toward compliance (§ 37.1302); (ii) the computation of projected operating costs (§ 37.1303); (iii) asset valuation requirements (§ 37.1304); (iv) a liquidity requirement for required

[33] 17 CFR 1.35(b)(5).

[34] *See* 17 CFR 1.31(d), 1.35(b)(5).

[35] 7 U.S.C. 7b-3(f)(13).

[36] *Id.*

financial resources equal to six months of a SEF's operating costs (§ 37.1305); and (v) reporting obligations (§ 37.1306).[37]

These regulations are intended to ensure that a SEF has financial strength sufficient to discharge its responsibilities, maintain market continuity, and withstand unpredictable market events.[38] Since the adoption of part 37 in 2013, the Commission received feedback from several SEFs noting the existing requirements impose impractical and unnecessary financial and operating burdens.[39] Among other things, SEFs contended the amount of financial resources a SEF is required to maintain has proven to be unnecessary and shackles resources that otherwise could be used towards operational growth and further innovation.[40] To address some of these concerns, Commission staff issued two guidance documents regarding the calculation of operating costs.[41]

Based on the Commission's experience with overseeing the financial resources requirements, feedback previously received from SEFs, and the Commission staff's experience with administering guidance on operating costs, the Proposed Rules set forth several amendments to the Core Principle 13 regulations, including the addition of acceptable practices to Core Principle 13 in Appendix B to part 37.[42] The intent of the

[37] 17 CFR 37.1301 through 37.1307.

[38] When the Commission adopted § 37.1301(a), it recognized that a SEF's financial strength is vital to ensure that the SEF can discharge its core principle responsibilities. SEF Core Principles Final Rule at 33538-33539.

[39] *See, e.g.*, WMBAA, Re: Project KISS at 5 (Sept. 29, 2017) ("2017 WMBAA Letter") *https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=61415&SearchText=*.

[40] *Id.* at 5.

[41] CFTC Staff Letter No. 17-25; CFTC Staff Letter No. 15-26.

[42] 83 FR at 62025-62030.

proposed amendments was to achieve a better balance between ensuring SEF financial stability and promoting SEF growth and innovation and reducing unnecessary costs.[43]

As discussed in greater detail below, the Proposed Rules included: (i) clarification of the scope of operating costs that a SEF must cover with adequate financial resources; (ii) acceptable practices for calculating projected operating costs; (iii) amendments to the existing six-month liquidity requirement for financial resources held by a SEF; and (iv) streamlined and flexible requirements with respect to financial reports filed with the Commission.

B. § 37.1301—General Requirements[44]

Existing § 37.1301(a) requires a SEF to maintain financial resources sufficient to enable it *to perform its functions in compliance* with the SEF core principles set forth in section 5h of the Act (emphasis added).[45] Existing § 37.1301(c) specifies that a SEF's financial resources shall be considered sufficient if their value is "at least equal to" the SEF's operating costs for a one-year period, calculated on a rolling basis.[46]

Certain SEFs expressed concerns that existing § 37.1301(a), when read in conjunction with existing § 37.1301(c), requires that SEFs include operational costs in the financial resources calculation, even if those costs relate to functions that are not

[43] *Id.* at 62025.

[44] In addition to finalizing the proposed amendments to § 37.1301(a) and (c), the Commission also proposed amendments to § 37.1301(b), which requires a SEF also operating as a DCO to comply with the financial resource requirements for DCOs under § 39.11. Specifically, the Commission proposed to amend § 37.1301(b) to permit a SEF that also operates as a DCO to file a single financial report under § 39.11 that covers both the SEF and DCO. The Commission is continuing to consider this proposed change and, therefore, is not finalizing it as part of the Final Rules.

[45] 17 CFR 37.1301(a).

[46] 17 CFR 37.1301(c).

germane to discharging SEF core principle responsibilities.[47] According to those SEFs, the requirement that SEFs maintain capital to cover such costs unnecessarily prevents SEFs from allocating that capital to operational growth and innovation.[48]

1. Proposed Rules

In the notice of proposed rulemaking, the Commission acknowledged some SEF operational costs may not be necessary to comply with a SEF core principle or Commission regulation and, therefore, should not be included when calculating the adequacy of the SEF's financial resources.[49] For example, a SEF may incur costs related to product research, business development, and advertising. Incurring costs to engage in these activities is unrelated to compliance with a SEF core principle or Commission regulation. Accordingly, the Commission proposed to eliminate § 37.1301(c), and instead amend § 37.1301(a) to require a SEF to maintain adequate financial resources to cover the operating costs of activities needed to "comply" with the SEF core principles, rather than "perform its functions in compliance with" the core principles.[50]

The Commission also proposed to amend § 37.1301(a) to require a SEF to maintain financial resources adequate to comply with "applicable Commission regulations." This amendment was intended to clarify that a SEF's obligation to maintain adequate financial resources extends to those resources necessary to comply with any

[47] *See* 2017 WMBAA Letter at 6 (stating the financial resource requirements should focus on fixed costs required for compliance, rather than variable costs and staff-related costs that are not essential).

[48] *Id.*

[49] 83 FR at 62025-62026.

[50] The Proposed Rules consolidated existing § 37.1301(a) and (c) into a single amended § 37.1301(a).

additional regulatory requirements the Commission has promulgated.[51] The Commission noted SEFs already are complying with this clarification in practice.[52]

Under proposed § 37.1301(a), a SEF need not maintain financial resources to cover the costs of activities (*e.g.*, product research, business development, or advertising) unrelated to compliance with a core principle or Commission regulation. The Commission stated the proposed rule offers a better and more balanced regulatory approach to implementing Core Principle 13 requirements, noting that under the proposed rule, SEFs would be able to allocate capital to other areas, thereby furthering the goals of promoting SEF growth and innovation.[53] Thus, the Commission concluded, the proposed rule would achieve a better balance between ensuring that a SEF is financially stable and providing the SEF discretion to allocate its limited resources towards growth and innovation.[54] Further, in proposing this rule, the Commission aimed to remove a potential barrier for new SEF entrants that might be deterred by the relatively higher capital costs required under existing regulations.[55]

The Commission also proposed several technical changes in order to align proposed § 37.1301(a) with Core Principle 13's requirements. Core Principle 13's requirements are ongoing, prompting the Commission to propose requiring a SEF to

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[51] This requirement is currently in effect, and the proposed rules simply clarified the requirement without substantively expanding it. Under Core Principle 1, a SEF must comply with any rule or regulation promulgated by the Commission pursuant to section 8a(5) of the Act. 17 CFR 37.100. For a SEF to discharge its responsibilities pursuant to Core Principle 13, which include complying with the SEF core principles, it is required to ensure that its financial resources are adequate to comply with those rules or regulations.

[52] 83 FR 62026.

[53] *Id.*

[54] *Id.*

[55] *Id.*

maintain adequate financial resources on an "ongoing basis." The Commission also proposed to replace the word "sufficient" with "adequate" while adopting additional language to specify a SEF's financial resources are "adequate" if their value "exceeds," rather than is "at least equal to," one year's worth of operating costs,[56] calculated on a rolling basis pursuant to the requirements for calculating such costs under proposed § 37.1303.

2. Summary of Comments

Refinitiv and WMBAA support the proposed changes to the general financial resource requirements.[57] They believe financial resources for certain SEF personnel and activities are not necessary for compliance with the SEF core principles or Commission regulations and the costs associated with these personnel and activities could be appropriately excluded in calculating projected operating costs.[58] WMBAA also believes the amendments will encourage SEF innovation and lower barriers to entry for new entities seeking to operate as SEFs.[59]

WMBAA requested the Commission allow a SEF to use a credit facility to meet the general financial resources requirement.[60] In addition, WMBAA stated the statutory

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[56] The Commission also proposed an amendment to refer to "projected operating costs" instead of "operating costs" to conform to existing § 37.1303, 17 CFR 37.1303, and § 37.1307, 17 CFR 37.1307, both of which refer to "projected operating costs." During informal discussions, Commission staff and SEFs generally have referred to SEFs' "projected operating costs."

[57] Refinitiv Letter at 13; 2019 WMBAA Letter at 21.

[58] *Id.*

[59] 2019 WMBAA Letter at 21.

[60] *Id*. In the preamble to the 2013 SEF Core Principles Final Rule, the Commission stated a SEF is allowed to include a credit facility to comply with the six-month liquid resources requirement (where its liquid assets on hand are insufficient) under § 37.1305, 17 CFR 37.1305, but otherwise is not allowed to include such a facility to demonstrate compliance with the one-year general requirement. 2013 SEF Core Principles Final Rule at 33540.

requirement a SEF maintain adequate financial resources to cover one year of operating costs is unnecessary and burdensome.[61] According to WMBAA, this amount of resources is not needed for a SEF to wind down its operations. Unlike futures contracts that are proprietary to, and traded exclusively on, a particular exchange, swaps of a particular type can and do trade on multiple SEFs, making it relatively easy to transfer trading to another SEF in the event of a wind-down.[62]

3. Final Rule

The Commission is adopting the amendments to § 37.1301(a) and eliminating § 37.1301(c) as proposed. The Commission believes it is unnecessary to require a SEF to maintain financial resources for activities beyond those required to comply with a SEF core principle or Commission regulation. Limiting the financial resources requirement to the costs of activities necessary to comply with the SEF core principles and Commission regulations is expected to reduce barriers to growth, innovation, and entry. The Commission believes this approach strikes an appropriate balance between ensuring a SEF's financial stability and allowing the SEF discretion in allocating resources.[63]

The Commission views WMBAA's request to permit the use of a credit facility to meet the general financial resources requirement as a substantive amendment to its regulations that is beyond the scope of the Proposed Rules. As a result, the Commission

[61] 2019 WMBAA Letter at 21.

[62] *Id.*

[63] This approach is consistent with the discretion granted to SEFs in the statutory core principles framework and other aspects of the Commission's financial resource requirements for SEFs. *See* 7 U.S.C. 7b-3(f)(1)(B) (granting a SEF reasonable discretion in establishing the manner in which it complies with the SEF core principles, unless the Commission provides otherwise by rule); 17 CFR 37.1303 (granting a SEF reasonable discretion in calculating its projected operating costs for purposes of 17 CFR 37.1301).

is not addressing the request in the Final Rules. However, the Commission may take the request into consideration for future rulemakings.

The Final Rules do not address WMBAA's comment that it is unnecessary and burdensome for a SEF to maintain financial resources covering a full year's operating costs, as this is a requirement set forth in the Act.[64]

C. § 37.1302—Types of Financial Resources

Existing § 37.1302 sets forth the types of financial resources available to a SEF to satisfy the general financial resources requirement.[65] These resources include the SEF's own capital, meaning its assets minus liabilities calculated in accordance with U.S. generally accepted accounting principles ("U.S. GAAP"), and any other financial resources deemed acceptable by the Commission.[66]

1. Proposed Rules

The Commission proposed to amend the current regulation to refer to generally accepted accounting principles "in the United States" in order to conform to the proposed amendments to § 37.1306 described further below.

2. Summary of Comments

The Commission received no comments on the proposed changes.

[64] 7 U.S.C. 7b-3(f)(13)(B) (providing that the financial resources of a swap execution facility shall be considered to be adequate if the value of the financial resources exceeds the total amount that would enable the swap execution facility to cover the operating costs of the swap execution facility for a 1-year period, as calculated on a rolling basis).

[65] 17 CFR 37.1302.

[66] *Id.*

3. Final Rules

The Commission is adopting the amendment to § 37.1302 as proposed. This change will conform to the adopted amendments to § 37.1306 described further below.

D. § 37.1303— Liquidity of Financial Resources

Existing § 37.1305 requires a SEF to maintain unencumbered, liquid financial assets, *i.e.*, cash and/or highly liquid securities, equal to at least six months of a SEF's operating costs.[67] If any portion of a SEF's financial resources is not sufficiently liquid, a SEF is permitted to take into account a committed line of credit or similar facility to meet this requirement.[68] In adopting this rule in 2013, the Commission explained that the liquidity requirement is intended to ensure that a SEF could continue to operate and wind down its operations in an orderly fashion, if necessary.[69] The Commission also determined that a six-month period would be an accurate assessment of how long it would take for a SEF to wind down in an orderly manner, absent support for alternative time frames.[70]

1. Proposed Rules

Since the adoption of part 37, many SEFs have maintained that a six-month minimum liquidity requirement is more than is necessary and some of their liquid assets

[67] 17 CFR 37.1305.

[68] *Id.*

[69] The Commission stated that the purpose of the liquidity requirement is so that all SEFs have liquid financial assets to allow them to continue to operate and to wind down in an orderly fashion and that the Commission viewed a six-month period as appropriate for a wind-down period. SEF Core Principles Final Rule at 33540.

[70] *Id.*

could be better applied toward growth of the SEFs.[71] Consistent with that feedback, the Commission observed that the wind-downs and ownership changes of several registered trading platforms, including SEFs and DCMs, were completed within much shorter time frames.[72] Based on this experience, the Commission acknowledged the existing six-month requirement is not necessary in all circumstances and a SEF may be better-positioned to determine the amount of liquid financial resources required to continue its operations and to conduct an orderly winddown.

In light of this experience, the Commission proposed to renumber § 37.1305 as § 37.1303 and amend the minimum liquid assets requirement to equal the greater of (i) three months of projected operating costs, calculated on a rolling basis; or (ii) the projected costs needed to wind down the swap execution facility's operations.[73] While recognizing that it rejected a three-month requirement in the SEF Core Principles Final Rule absent support for a shorter time frame,[74] the Commission stated it had since come to believe, based on its experience and the feedback discussed above, that the potentially shorter proposed time frame would be sufficient to fulfill the goal of ensuring a SEF can continue to operate and, if necessary, wind down its SEF operations in an orderly fashion.[75]

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[71] *See* 2017 WMBAA Letter at 5 (arguing a shorter liquidity requirement would allow for a SEF to allocate capital for innovation).

[72] For example, the Commission noted that the DCM Green Exchange LLC had its designation vacated and ceased operations. Similarly, the DCM Kansas City Board of Trade was acquired by CME Group Inc. and had its designation vacated; it ultimately ceased operations. In each case, the Commission observed a relatively expeditious process.

[73] 83 FR at 62027.

[74] SEF Core Principles Final Rule at 33540.

[75] 83 FR at 62027.

The Commission further noted that under the proposed change, SEFs would be able to use the resources previously allocated to the liquid asset requirement to invest in other areas of SEF operations.[76] Accordingly, compared to the existing static six-month requirement, the Commission stated a liquid resources requirement of the "greater of" either (i) three months of projected operating costs or (ii) projected wind-down costs better ensures an orderly wind down for SEFs and a more efficient allocation of resources for SEFs estimating a wind-down period less than six months.[77] The Commission further stated requiring SEFs to maintain the greater of three months of projected operating costs or the SEF's projected costs for an orderly wind down of its business better protects against the risk of failure in the unlikely event that a SEF requires a wind-down period of longer than six months.[78]

The Commission also proposed an amendment to clarify that a SEF can overcome any deficiency in satisfying this requirement by obtaining a committed line of credit or similar facility in an amount at least equal to the deficiency.

2. Summary of Comments

Refinitiv and Bloomberg support the proposed rule and believe the proposed three-month minimum liquid asset requirement better reflects a SEF's liquidity needs for day-to-day operations and, if necessary, for winding down operations.[79] Refinitiv supports focusing the liquid financial resources requirement on the cost of unwinding the

[76] *Id.*

[77] *Id.*

[78] *Id.*

[79] Refinitiv Letter at 13; Bloomberg Letter at A-6.

SEF in an orderly manner.[80] Bloomberg believes a SEF's wind-down period will generally be no more than three months and that the revised liquidity requirement "will release capital that can be deployed by a SEF to promote innovation, while also promoting stability by ensuring that a SEF retains sufficient capital on reserve."[81]

WMBAA requested the Commission allow SEFs to count all commissions receivable, aged less than three months, towards their liquid financial resources calculation.[82] WMBAA believes permitting the use of liquid receivables would not impair a SEF's ability to perform its core functions, but would enable a SEF to avoid locking up cash unnecessarily. According to WMBAA, payment of these commissions typically occurs within one to two months, and thus would be available to cover operating costs or a wind-down.[83] WMBAA also urged the Commission to allow revolving subordinated debt as a liquid asset in the financial resource requirement.[84]

3. Final Rules

The Commission is adopting § 37.1303 as proposed. Requiring a SEF to maintain liquid financial resources equal to the greater of three months of projected operating costs or its projected wind-down costs will ensure that SEFs have sufficient resources for day-to-day operations as well as winding down operations if needed, while freeing capital for innovation and expansion in the SEF's business where appropriate.

[80] Refinitiv Letter at 13.

[81] Bloomberg Letter at A-6.

[82] 2019 WMBAA Letter at 21.

[83] *Id.*

[84] *Id.*

The Commission notes that under existing § 37.1303, amended as § 37.1304, the Commission may review the methodologies used in the calculation of a SEF's projected costs needed to wind down the swap execution facility's operations and may require changes as appropriate. Some examples a SEF may use to support its conclusion include: the tenor of the contracts listed on the facility, the listing of the SEF's contracts on other facilities, the ability of participants to close out positions and trade on a different SEF and, in the event the SEF's swaps are cleared, the ability of participants to clear swaps at the same DCO as they currently utilized if they had to trade on a different facility.

Finally, WMBAA's requests to include additional types of resources as liquid assets are beyond the scope of this rulemaking. The Commission may consider including additional types of liquid assets in a future rulemaking.

E. § 37.1304—Computation of Costs to Meet Financial Resources Requirement[85]

Existing § 37.1303 requires a SEF to make a reasonable calculation of its projected operating costs, each fiscal quarter over a twelve-month period, to determine the amount of financial resources needed to comply with the financial resource requirement.[86] The rule further provides a SEF reasonable discretion to determine the methodology to compute its projected operating costs, although the Commission may review the SEF's methodology and require the SEF to make changes as appropriate.[87]

[85] The Commission is renaming this section, previously titled "Computation of Projected Operating Costs to Meet Financial Resource Requirement," to reflect the requirement to calculate wind-down costs as well as operating costs.

[86] 17 CFR 37.1303.

[87] *Id.*

1. Proposed Rules and Acceptable Practices

The Commission proposed to renumber § 37.1303 as § 37.1304 and amend the rule to add the requirement that a SEF make a reasonable calculation of projected wind-down costs, providing discretion in adopting the methodology for calculating such costs. The Commission stated the proposed amendment is consistent with the reasonable discretion already provided for calculating projected operating costs and corresponds to proposed § 37.1303, which incorporates the calculation of a SEF's wind-down costs into the liquidity determination.[88] The Commission proposed two additional amendments to § 37.1303. First, the Commission proposed to add a reference to amended § 37.1303 to require that a SEF calculate projected operating costs to determine how to comply with the liquidity requirement. Second, the Commission proposed to eliminate the reference to the twelve-month requirement, given that proposed § 37.1301(a) establishes that the financial resource requirement applies on a one-year, rolling basis.

The Commission also proposed to include acceptable practices to Core Principle 13 in Appendix B associated with proposed § 37.1304. The proposed acceptable practices expound upon the reasonable discretion that SEFs have for computing projected operating costs in determining their financial resource requirements, consistent with existing guidance provided by Commission staff.[89] Among other things, these acceptable practices further explain which operating costs are not necessary to comply with the SEF

[88] 83 FR 62028.

[89] The proposed acceptable practices to Core Principle 13 in Appendix B are based, in part, upon existing Division of Market Oversight ("DMO") staff guidance. *See* CFTC Staff Letter No. 15-26 and CFTC Staff Letter No. 17-25.

core principles and the Commission's regulations and therefore need not be considered in a SEF's financial resources calculation under revised § 37.1301.

Specifically, the proposed acceptable practices state that calculations of projected operating costs, *i.e.*, those that are necessary for a SEF to comply with the SEF core principles and applicable Commission regulations, should be based on the SEF's current business model and anticipated business volume. The proposed acceptable practices specify that a SEF may exclude certain expenses in making a "reasonable" calculation of projected operating costs. These include, among others, the following expenses: marketing and development costs; variable commissions paid to SEF trading specialists, the payment of which is contingent on whether the SEF collects associated revenue from transactions on its systems or platforms;[90] and costs for SEF personnel who are not necessary to enable a SEF to comply with the core principles and Commission regulations.[91] Further, a SEF may exclude any non-cash costs, including depreciation and amortization. The exclusion of these expenses is consistent with the financial resource and liquidity requirements in proposed § 37.1301 because these expenses are not necessary for a SEF to comply with the SEF core principles or Commission regulations.

In addition, the proposed acceptable practices specify that a SEF in calculating projected operating costs may prorate, but not exclude, certain expenses. The Commission recognizes some costs may be only partially attributable to a SEF's compliance with the SEF core principles and regulatory requirements. Therefore, only

[90] *See* CFTC Staff Letter No. 17-25.

[91] For example, if a SEF requires a certain number of SEF trading specialists to operate a voice-based or voice-assisted trading system or platform, but hires additional personnel to enhance its operations to benefit market participants, then the SEF would only need to include the minimum number of trading specialists required to operate the trading system or platform based on its current business volume and take into account any projected increase or decrease in business volume in its projected operating cost calculations.

those attributed costs need to be included in a SEF's projected operating costs. Accordingly, a SEF may prorate expenses shared with affiliates, *e.g.*, the costs of administrative staff or seconded employees the SEF shares with affiliates. Further, a SEF may also prorate expenses that are attributable, in part, to operational aspects of the SEF business that are not required to comply with the SEF core principles, *e.g.*, costs of a SEF's office space, to the extent that it is also used to house marketing personnel. In prorating any such expense, however, a SEF must document and justify those prorated expenses pursuant to proposed requirements under proposed § 37.1306, discussed further below.[92]

2. Summary of Comments

WMBAA supports the proposed acceptable practices.[93] Refinitiv concurs with the Commission's understanding that many SEF expenses are shared with affiliates or are partly attributable to activities not necessary for compliance with the SEF core principles and Commission regulations and supports allowing SEFs to prorate such expenses.[94]

[92] The proposed acceptable practices also allowed a SEF offering more than one bona fide execution method to include the costs of only one of those methods in calculating projected operating costs, with the goal of mitigating disincentives for SEFs to offer a multiplicity of execution methods. This proposed change was intended to be consistent with the Proposed Rule's removal of existing limitations on execution methods for Required Transactions. Because the Final Rules are not implementing the Proposed Rule's expansion of permissible execution methods for Required Transactions, the Commission is not finalizing this proposed acceptable practice at this time.

[93] 2019 WMBAA Letter at 22. WMBAA requested that the Commission clarify the meaning of "bona fide" execution method for purposes of calculating operating costs of SEF execution methods. As noted above, the Commission at this time is not finalizing the proposed acceptable practice regarding treatment of operating costs for multiple execution methods.

[94] *See* Refinitiv Letter at 13-14.

3. Final Rules and Acceptable Practices

The Commission is adopting § 37.1304 and the acceptable practices as proposed. The requirement to calculate wind-down costs corresponds to the amendments the Commission is adopting in amended § 37.1303 discussed above, which incorporate the calculation of a SEF's wind-down costs into the liquidity requirement. The reasonable discretion provided for calculation of wind-down costs is already provided to SEFs for their calculations of projected operating costs.

The Commission believes the acceptable practices added to Appendix B to part 37 will assist SEFs in complying with amended § 37.1304.[95] These acceptable practices are consistent with the Final Rules' amendments to § 37.1301, which focus a SEF's financial resource requirement on covering the costs of compliance with SEF statutory and regulatory obligations, rather than the costs of *all* operations of a SEF or operations of its affiliates.

F. § 37.1305—Valuation of Financial Resources

Existing § 37.1304—"Valuation of financial resources"—requires a SEF, at least once each fiscal quarter, to compute the current market value of each financial resource used to meet its financial resources requirement under § 37.1301.[96] The requirement is designed to address the need to update valuations when there may have been material fluctuations in market value that could affect a SEF's ability to satisfy its financial

[95] As noted, the Commission at this time is not finalizing the proposed acceptable practice allowing a SEF offering multiple bona fide execution methods to count the costs of only one execution method toward its projected operating costs, for the reasons stated above. *See* note 92, *supra*.

[96] 17 CFR 37.1304.

resource requirement.[97] When valuing a financial resource, the SEF must reduce the value, as appropriate, to reflect any market or credit risk specific to that particular resource, *i.e.*, apply a haircut.[98]

1. Proposed Rules

The Commission proposed to renumber existing § 37.1304 as § 37.1305 and amend the provision to add a reference to the liquidity requirement under amended § 37.1303. This would clarify that compliance with amended § 37.1303 requires a SEF to utilize the current market value of the applicable financial resources as computed pursuant to § 37.1304.

2. Summary of Comments

The Commission did not receive any comments on this amendment.

3. Final Rules

The Commission is adopting § 37.1305 as proposed, confirming that compliance with the liquidity requirement under amended § 37.1303 requires a SEF to utilize the current market value of the applicable financial resources.

G. § 37.1306—Reporting to the Commission

1. § 37.1306(a)

Existing § 37.1306 establishes a SEF's financial reporting requirements.[99] Commission regulation 37.1306(a)(1) provides that at the end of each fiscal quarter or upon Commission request, a SEF must report to the Commission (i) the amount of

[97] SEF Core Principles Final Rule at 33539.

[98] A "haircut" is a deduction taken from the value of an asset to reserve for potential future adverse price movement in such asset. *Id.* at 33539 n.772.

[99] 17 CFR 37.1306.

financial resources necessary to meet the financial resources requirement of § 37.1301, and (ii) the value of each financial resource available to meet those requirements as calculated under § 37.1304.[100] Commission regulation 37.1306(a)(2) additionally requires a SEF to provide the Commission each fiscal quarter with a financial statement, including a balance sheet, income statement, and statement of the cash flows of the SEF or its parent company.[101] In lieu of submitting its own financial statements, a SEF may submit the financial statements of its parent company.[102]

i. Proposed Rules

The Commission proposed several amendments to § 37.1306(a). First, the Commission proposed to require a SEF to prepare its financial statements in accordance with U.S. GAAP. For a SEF that is not domiciled in the U.S., and is not otherwise required to prepare its financial statements in accordance with U.S. GAAP, the Proposed Rules allowed the SEF to prepare its statements in accordance with either the International Financial Reporting Standards issued by the International Accounting Standards Board, or such comparable international standard as the Commission may accept in its discretion. The Commission noted the quality and transparency of SEF financial reports submitted under the current reporting requirement have varied and stated the U.S. GAAP-based requirement would promote consistency and better ensure a minimum reporting standard across financial submissions.[103]

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[100] 17 CFR 37.1306(a)(1).

[101] 17 CFR 37.1306(a)(2).

[102] *Id.*

[103] 83 FR 62029.

The Commission also proposed to require a SEF to provide its own financial statements, rather than allow a SEF the option of submitting the statements of its parent company. The Commission noted it may lack jurisdiction over a SEF's parent company or its affiliates, and in such instances, the Commission could not consider the parent company's financial resources in determining whether the SEF alone possesses adequate financial resources.[104] The Commission stated a separate SEF financial statement would more clearly demonstrate evidence of the SEF's compliance with Core Principle 13.[105]

The Commission also proposed revisions to § 37.1306(a)(1) to add appropriate references to amended § 37.1303 and amended § 37.1305. In addition to specifying the amount of financial resources necessary to comply with § 37.1301, a SEF's quarterly report would have to include the amount of financial resources necessary to comply with the liquidity requirement in amended § 37.1303. Further, the amounts specified in the report would have to be based on the current market value of each financial resource and computed as reasonable calculations of the SEF's projected operating costs and wind-down costs.

The Proposed Rules also posed several questions to commenters on reporting requirements for SEFs. These included whether a SEF's financial reports should be required to be audited and whether financial reporting should be required on a semiannual rather than a quarterly basis.

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[104] *Id.*

[105] *Id.*

ii. Summary of Comments

WMBAA supports requiring a SEF's financial statements be prepared in accordance with U.S. GAAP or its equivalent for non-U.S. SEFs, concurring with the Commission's view that such a requirement would promote comparability across SEFs.[106]

WMBAA objects to requiring a SEF's financial reports be audited, contending audited reports would not improve oversight. WMBAA reasoned that an auditing firm would not provide a complete assessment because it likely would be unable or unwilling to opine on certain unique aspects of a SEF's financial resources calculations, including projection of costs based on historical or estimated costs.[107] Further, WMBAA argued the costs associated with an audited report are high and would pose a barrier to entry for new SEFs.[108]

WMBAA also believes the current reporting requirement—quarterly financial reports—is sufficient to ensure capital adequacy, but that a semi-annual and annual report would also be adequate to achieve the goal of Commission oversight.[109] According to WMBAA, if the Commission adopts less frequent financial reporting, a SEF should be required to maintain all related documents and support for further inspection.[110] However, WMBAA asserted a SEF should not be required to maintain, in between each

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[106] WMBAA Letter at 23.

[107] *Id*. at 22. WMBAA also stated that an auditing firm would be unlikely to opine on whether an execution method is "bona fide" for purposes of the proposed acceptable practices related to § 37.1303. As noted above, the meaning of "bon fide" is not relevant since the Commission is not finalizing the proposed acceptable practice regarding the calculation of costs of different execution methods.

[108] *Id*.

[109] *Id*. at 22-23.

[110] *Id*. at 22.

report, the supplemental documents required under existing § 37.1306(c).[111] Rather, WMBAA contends a SEF should be able to maintain a balance sheet with financial resources and liquidity calculations based on the most recent filing.[112]

The Commission did not receive any comments on its proposal to require SEFs to submit their own financial statements rather than those of their parent entities.

iii. Final Rules

The Commission is adopting the proposal requiring financial statements submitted as part of a SEF's quarterly financial reports to conform to U.S. GAAP or comparable foreign standards. As supported by commenters' feedback, the Commission continues to believe conforming financial statements to U.S. GAAP or comparable foreign standards will enhance the quality and transparency of SEFs' financial reporting and facilitate assessments of SEFs' financial conditions.

The Commission is adopting, as proposed, the requirement for a SEF to provide its own financial statements (including balance sheet), rather than the financial statements of its parent. This change will provide the Commission with a more accurate picture of the SEFs' assets to ensure a SEF has adequate financial resources.[113]

The Commission will not adopt the requirement that financial statements be audited. As noted by commenters, the Commission has the ability to request additional

[111] Existing § 37.1306(c) requires a SEF to provide the Commission with supplemental documentation to its quarterly reports, including documentation used to calculate its financial requirements; documentation showing the basis for financial resource valuations and liquidity requirements; and copies of relevant agreements supporting the SEF's calculations.

[112] WMBAA Letter at 22.

[113] The Commission is finalizing the amendments to § 37.1306(a)(1) as proposed.

information from a SEF if warranted, and the Commission does not believe the benefits of a blanket auditing requirement would justify the costs to SEF operators at this time.

Finally, the Commission will retain the existing quarterly reporting requirement for SEFs, rather than moving to a semiannual reporting requirement. Quarterly reports are necessary for the Commission to remain current with the SEF's financial condition in a manner that semiannual reports would not. Timely financial information will be particularly important to the Commission as it monitors the transition to a relatively less stringent liquidity requirement for SEFs' financial resources under the Final Rules.[114]

2. § 37.1306(c)[115]

Existing § 37.1306(c) sets forth documentation requirements for a SEF's financial reporting obligations.[116] Commission regulation 37.1306(c)(1) requires a SEF to provide the Commission with sufficient documentation explaining the methodology used to calculate its financial resource requirements under § 37.1301.[117] Commission regulation 37.1306(c)(2) requires a SEF to provide sufficient documentation explaining the basis for its valuation and liquidity determinations.[118] To provide such documentation, § 37.1306(c)(3) requires SEFs to provide copies of certain agreements that evidence or otherwise support its conclusions.[119]

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[114] *See* Section III.D., *supra*.

[115] Existing § 37.1306(b), 17 CFR 37.1306(b), requires a SEF to make its financial resource calculations on the last business day of its fiscal quarter. The Commission proposed an amendment to § 37.1306(b) adding the word "applicable" before "fiscal quarter" in the existing rule text. The Commission is finalizing this amendment as proposed.

[116] 17 CFR 37.1306(c).

[117] 17 CFR 37.1306(c)(1)

[118] 17 CFR 37.1306(c)(2).

[119] 17 CFR 37.1306(c)(3).

i. Proposed Rules

Based on the proposed amendments to the Core Principle 13 regulations described above, the Commission proposed conforming amendments to § 37.1306(c) that would require a SEF to specify the methodology used to compute its financial resources and liquidity requirements. Proposed § 37.1306(c)(1) requires documentation to be sufficient to enable the Commission to determine whether the SEF has made reasonable calculations of projected operating and wind-down costs under § 37.1303. Proposed § 37.1306(c)(2)(i) through (iv)[120] requires the SEF, at a minimum, to (i) list all of its expenses, without exclusion; (ii) identify all of those expenses the SEF excluded or prorated in its projected operating cost calculations and explain the basis for excluding or prorating any expenses; (iii) include documentation related to any committed line of credit or similar facility used to meet the liquidity requirement;[121] and (iv) identify estimates of all of the costs and the projected amount of time required for any wind down of operations, including the basis for those estimates.

The proposed requirement would create regulatory certainty by codifying the no-action relief, permitting SEFs to maintain their existing practices and avoid legal exposure arising out of a SEF's inability to comply with regulations.[122] The proposed requirements would ensure that a SEF can establish that it has sufficient financial

[120] The Commission proposed to consolidate § 37.1306(c)(1) through (3) into § 37.1306(c)(1) through (2) and adopt the proposed requirements as described.

[121] The Commission also proposed to eliminate the language in existing § 37.1306(c)(3) regarding copies of insurance coverage or other arrangements evidencing or otherwise supporting the SEF's conclusions. The Commission noted that proposed § 37.1306(c) requires a SEF to provide sufficient documentation explaining the methodology used to compute its financial resource requirements. Therefore, if insurance coverage or other arrangements are necessary to explain a SEF's methodology, then the SEF must submit such documentation. The Commission noted, however, that such documentation may not be required in all cases; proposed § 37.1306(c)(2) provides minimum requirements.

[122] *See* CFTC Staff Letter No. 17-25 at 4.

resources, particularly in light of the discretion provided to SEFs to compute projected operating costs and wind-down costs. The Commission noted its belief that maintaining the general obligation for each SEF to identify all of its expenses in its financial report, including those corresponding to activities not needed for compliance or otherwise are excluded or prorated from projected operating costs, is appropriate on an ongoing basis.[123]

The Commission further stated proposed § 37.1306(c)(2)(i) through (iv) would address the current lack of adequate documentation or insufficient identification of excluded or prorated expenses by some SEFs in submitting their projected operating costs based on Commission staff guidance.[124] The Commission predicted that adding greater specificity to the existing requirement would mitigate the time and resources required to determine a SEF's compliance with the financial resources requirements.[125]

ii. Summary of Comments

The Commission did not receive any comments on the proposed amendments to § 37.1306(c).

iii. Final Rules

The Commission is adopting the amendments to § 37.1306(c) as proposed. The enhanced specificity in documentation requirements will save time and effort for both Commission and SEF personnel by reducing the need for multiple iterations of communications and submissions in order to assess a SEF's compliance with the financial resources requirements. The requirement to provide documentation of projected

[123] 83 FR 62030.

[124] *Id.*

[125] *Id.*

wind-down costs corresponds to the incorporation under the revised rules of wind-down costs into a SEF's liquidity requirement and the requirement to compute such costs in addition to operating costs.

3. § 37.1306(d)

Existing § 37.1306(d) requires a SEF to file its financial report no later than 40 calendar days after the end of each of the SEF's first three fiscal quarters, and no later than 60 calendar days after the end of the SEF's fourth fiscal quarter, or at such later time as the Commission may permit.[126] Multiple SEFs noted difficulties in meeting the 60-day deadline for the fourth-quarter report, explaining: "[a]t year end, finance departments are required to prepare annual and quarterly reports for all entities within a particular group. This requires information gathering from numerous sources, preparation of a consolidated audit, complying with various statutory reporting requirements, as well as budgeting and forecasting for the pending year."[127] Noting the difficulties SEFs face in meeting their obligation to submit an annual compliance report concurrently with the fourth-quarter financial report, Commission staff provided no-action relief allowing 30 additional days for submission of a SEF's fourth-quarter financial report and its annual compliance report.[128]

i. Proposed Rules

The Commission proposed to extend the due date for SEFs' fourth-quarter report from 60 to 90 days following the end of the quarter. The revised due date would conform

[126] 17 CFR 37.1306(d).

[127] CFTC Staff Letter No. 17-61 (Nov. 20, 2017) (quoting no-action relief request letter from 360 Trading Networks, Inc.; Cboe SEF, LLC (f/d/b/a Bats Hotspot SEF, LLC); Chicago Mercantile Exchange, Inc.; GTX SEF, LLC; LatAm SEF, LLC; LedgerX LLC; Tradition SEF, Inc.; and trueEX LLC).

[128] *Id.*

to the proposed revisions to the due date for the SEF annual compliance report under proposed § 37.1501(e)(2), discussed below. The Commission recognized that preparing multiple year-end reports for concurrent submission, including a fourth-quarter financial report and an annual compliance report, imposes resource constraints on SEFs.[129] The Commission stated such potential constraints justify an additional 30 days to prepare and concurrently file the SEF's fourth-quarter financial report along with its annual compliance report.[130]

ii. Summary of Comments

The Commission did not receive any comments on the proposed extension of the deadline for submission of the fourth-quarter financial report.

iii. Final Rules

The extended deadline for fourth-quarter financial reports is being adopted as proposed. The Commission continues to believe the resource constraints facing SEFs at year-end justify an additional 30 days to prepare the fourth-quarter financial report. The Commission has not experienced difficulties in monitoring SEFs' financial condition as a result of the 30-day extension currently available under Commission staff no-action relief.

4. § 37.1306(e)

i. Proposed Rules

The Commission proposed to add a new § 37.1306(e) requiring each SEF to provide notice to the Commission of its noncompliance with the financial resource

[129] 83 FR 62030.

[130] *Id*.

requirements no later than 48 hours after the SEF knows or reasonably should know of its noncompliance.[131] The Commission noted that in some instances, the Commission has not been informed of a SEF's noncompliance with the financial resource requirements until the filing of a quarterly financial report. Prompt notification of noncompliance is necessary for the Commission to conduct proper market oversight and ensure market stability on an ongoing basis.[132] The proposed requirement would ensure the necessary prompt notification.

ii. Summary of Comments

The Commission did not receive any comments on proposed § 37.1306(e).

iii. Final Rules

The Commission is adopting § 37.1306(e) as proposed. The Commission continues to believe prompt notification of noncompliance is necessary for it to perform its oversight functions and ensure market stability.

H. § 37.1307—Delegation of Authority

Existing § 37.1307(a) delegates authority to the Director of DMO, or other staff as the Director may designate, to perform certain functions that are reserved to the Commission under the Core Principle 13 regulations, including reviewing the methodology used to compute projected operating costs.[133]

[131] For example, if a SEF knows or reasonably should know that its assets will no longer cover its projected operating costs for the next twelve months, as calculated on a rolling basis, the SEF would be required to notify the Commission within 48 hours.

[132] 83 FR 62030.

[133] 17 CFR 37.1307(a).

1. Proposed Rules

The Commission proposed to amend § 37.1307(a)(2) to additionally delegate the authority to review and make changes to the methodology used by a SEF to determine the market value of its financial resources under amended § 37.1304 and the methodology that SEFs use to determine their wind-down costs under amended § 37.1305. Further, the Commission would delegate the ability to request and receive the additional documentation related to calculation methodologies required under § 37.1306(c) and receive required notifications of noncompliance under § 37.1306(e). The proposed amendments also include several additional technical amendments based on the proposed amendments to Core Principle 13 regulations, as described above.

2. Summary of Comments

The Commission did not receive any comments on the proposed delegations of authority.

3. Final Rules

The Commission is adopting the additional provisions for delegation of authority as proposed. These delegation provisions will facilitate prompt and efficient determinations of the adequacy of SEF financial resources, consistent with the existing delegation authority under § 37.1307(a).

IV. Chief Compliance Officer Requirements

A. Background and Overview of Proposed Rules

Statutory Core Principle 15 requires each SEF to designate a CCO and sets forth its corresponding duties.[134] Among other responsibilities, the CCO is required to ensure

[134] 7 U.S.C. 7b-3(f)(15). The Commission codified Core Principle 15 under § 37.1500. 17 CFR 37.1500.

that the SEF complies with the CEA and applicable rules and regulations, and is required to establish and administer required policies and procedures.[135] Core Principle 15 also requires the CCO to prepare and file an ACR to the Commission.[136] The Commission promulgated requirements under § 37.1501 to implement these requirements.[137]

The Proposed Rules set forth several amendments to § 37.1501 based on the Commission's experience since the part 37 implementation. These amendments streamline CCO requirements, allow SEF management to exercise discretion in CCO oversight, and simplify the preparation and submission of the ACR.

B. § 37.1501(a)—Definitions

Core Principle 15 requires the CCO to report directly to the SEF's "board [of directors]" or "senior officer"[138] and consult either to resolve conflicts of interest.[139] Existing § 37.1501(a) defines "board of directors"[140] but does not define "senior officer."[141] In the SEF Core Principles Final Rule, the Commission stated it would not adopt a definition of "senior officer," but noted the statutory term would only include the most senior executive officer of the legal entity registered as a SEF.[142]

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[135] 7 U.S.C. 7b-3(f)(15)(B)(iv) through (v).

[136] 7 U.S.C. 7b-3(f)(15)(D).

[137] 17 CFR 37.1501.

[138] 7 U.S.C. 7b-3(f)(15)(B)(i).

[139] 7 U.S.C. 7b-3(f)(15)(B)(iii).

[140] Section 37.1501(a) defines "board of directors" as the board of directors of a SEF, or for those SEFs whose organizational structure does not include a board of directors, a body performing a function similar to a board of directors. 17 CFR 37.1501(a).

[141] 17 CFR 37.1501(a). The CEA likewise does not define the term "senior officer" in this context.

[142] SEF Core Principles Final Rule at 33544.

1. Proposed Rules

The Commission proposed to relabel paragraph (a) as "Definitions," and define "senior officer" as the chief executive officer or other equivalent officer of the SEF. The Commission stated defining "senior officer" would clarify the permissible reporting lines for the CCO and provide specificity to the Commission's proposed amendments to the Core Principle 15 regulations, as described below.[143] The Commission also proposed additional, technical changes.

2. Summary of Comments

WMBAA supports the proposed amendments to add a definition of senior officer.[144]

3. Final Rules

The Commission is adopting § 37.1501(a) as proposed. The Commission continues to believe the definition of senior officer will clarify a CCO's permissible reporting lines consistent with Core Principle 15.

C. § 37.1501(b)— Chief Compliance Officer

Existing §§ 37.1501(b)-(c) set forth certain baseline requirements for the SEF CCO position. Commission regulation 37.1501(b)—"Designation and qualifications of chief compliance officer"— requires a SEF to designate an individual to serve as the CCO; requires the CCO to have the authority and resources to help fulfill the SEF's statutory and regulatory duties, including supervisory authority over compliance staff; and establishes minimum qualifications for the designated CCO.[145] Commission

[143] 83 FR 62023.

[144] 2019 WMBAA Letter at 23.

[145] 17 CFR 37.1501(b).

regulation 37.1501(c)—"Appointment, supervision, and removal of chief compliance officer"—establishes the respective authorities of the SEF board of directors and senior officer to designate, supervise, and remove a CCO; and requires the CCO to meet with the SEF's board of directors and regulatory oversight committee ("ROC") on an annual and quarterly basis, respectively, and provide them with information as requested.[146]

1. Proposed Rules

The Commission proposed to amend, clarify, or eliminate various existing requirements under § 37.1501(b) and (c) and consolidate the remaining provisions into § 37.1501(b). The Commission proposed to eliminate rules that are duplicative of Core Principle 15, including requirements that a SEF designate a CCO[147] and the CCO report directly to the board of directors or the senior officer.[148] The Commission also proposed to eliminate the existing ROC-related requirements from part 37.[149] Core Principle 15 does not require a SEF to establish a ROC and the Commission has not finalized a rule that establishes requirements for a ROC.

Consistent with Core Principle 15, which requires a CCO to report to the SEF's board of directors or senior officer, the Commission proposed amendments under § 37.1501(b) to allow a SEF's senior officer to have the same oversight responsibilities

[146] 17 CFR 37.1501(c).

[147] The Commission proposed to eliminate this requirement under existing § 37.1501(b)(1), which the Commission proposed to retitle "Authority of chief compliance officer" from "Chief compliance officer required."

[148] The Commission proposed to eliminate this requirement under existing § 37.1501(c)(2) because it is duplicative of statutory Core Principle 15.

[149] These requirements include a mandatory quarterly meeting with the ROC under existing § 37.1501(c)(1)(iii), and the requirement that the CCO provide self-regulatory program information to the ROC under existing § 37.1501 (c)(1)(iv).

over the CCO as the board of directors. First, the Commission proposed to allow a CCO to consult with the board of directors or senior officer of the SEF as the CCO develops the SEF's policies and procedures.[150] Second, the Commission proposed to allow a CCO to meet with the senior officer of the SEF on an annual basis, in lieu of an annual meeting with the board of directors.[151] Third, the Commission proposed to allow a CCO to provide self-regulatory program information to the SEF's senior officer, in addition to the board of directors.[152]

The Commission further proposed to eliminate the limitations on authority to remove a CCO, which currently restricts CCO removal authority to a majority of the board, or in the absence of a board, a senior officer.[153] Instead, the Commission proposed a simplified requirement under proposed § 37.1501(b) to establish that (i) the board or the senior officer may appoint or remove a CCO;[154] and (ii) the SEF must notify the Commission within two business days of the appointment or removal (on an interim or

[150] The Commission proposed the amendment under proposed § 37.1501(b)(1)(i).

[151] The Commission proposed to renumber existing § 37.1501(c)(1)(iii) to § 37.1501(b)(5), based on the proposed consolidation of existing paragraphs (b) and (c), amend the requirement as described, and title the paragraph "Annual meeting with the chief compliance officer."

[152] The Commission proposed to renumber existing § 37.1501(c)(1)(iv) to § 37.1501(b)(6), based on the proposed consolidation of existing paragraphs (b) and (c), amend the requirement as described, title the paragraph "Information requested of the chief compliance officer," and make additional, technical changes.

[153] The Commission proposed to eliminate this requirement under existing § 37.1501(c)(3). In addition to the changes discussed herein, the Commission proposed to renumber existing § 37.1501(c)(1)(ii) to § 37.1501(b)(4) and title the paragraph "Compensation of the chief compliance officer."

[154] The Commission proposed to consolidate and amend the requirements under existing § 37.1501(c)(1)(i) in part, which addresses the appointment of a CCO by the board or senior officer, with existing § 37.1501(c)(3)(i), which currently addresses the removal of a CCO. Based on the proposed consolidation of existing paragraphs (b) and (c), the Commission proposed to renumber this consolidated provision to paragraph (b)(3), retitle the consolidated provision to "Appointment and removal of chief compliance officer," and make additional, technical changes.

permanent basis) of a CCO.[155] Based on its experience, the Commission recognized that in many instances, the senior officer may be better positioned than the board of directors to provide day-to-day oversight of the SEF and the CCO, as well as to determine whether to remove a CCO.[156] Therefore, consistent with Core Principle 15, the Commission believes a SEF's senior officer should have equivalent CCO oversight authority as the SEF's board of directors. This proposed amendment is consistent with Core Principle 15, which does not mandate a voting percentage to approve or remove a CCO. The Commission also believes these proposed amendments would allow a SEF to more appropriately designate, appoint, supervise, and remove a CCO based on the SEF's particular corporate structure, size, and complexity, and also continue to ensure a level of independence for a CCO consistent with Core Principle 15.[157]

Based on the proposed consolidation of existing § 37.1501(b) and (c), the Commission also proposed several technical amendments to the remaining provisions under proposed § 37.1501(b), including the renumbering of certain existing provisions.[158]

2. Proposed Acceptable Practice

The Commission proposed to adopt a new acceptable practice to Core Principle 15 in Appendix B providing, in determining whether the background and skills of a

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[155] The Commission notes that notification to the Commission of the appointment and removal of a CCO is currently required under existing § 37.1501(c)(1)(i) and existing § 37.1501(c)(3)(ii), respectively. Based on the proposed consolidation of existing paragraphs (b) and (c), the Commission proposed to consolidate and amend these notification requirements, and renumber the consolidated requirement to § 37.1501(b)(3)(i).

[156] 83 FR 62033.

[157] *Id.*

[158] The Commission proposed to renumber the requirements under existing § 37.1501(b)(2)—"Qualifications of chief compliance officer"—to proposed § 37.1501(b)(2)(i) and (ii). The Commission also proposed to retitle existing § 37.1501(c)(1)(ii), which specifies that the board or the senior officer must approve the CCO's compensation, to "Compensation of the chief compliance officer." Based on the proposed consolidation of existing § 37.1501(b) and (c), the Commission proposed to renumber this requirement to § 37.1501(b)(4).

potential CCO are appropriate for fulfilling the responsibilities of the role of the CCO, a SEF has the discretion to base its determination on the totality of the qualifications of the potential CCO, including, but not limited to, compliance experience, related career experience, training, and any other relevant factors related to the position. The Commission stated a non-exclusive list provides the clarity that SEFs sought regarding a CCO's requisite qualifications, and also provides a board of directors and senior officer reasonable flexibility in appointing a CCO.[159] The proposed acceptable practice also states a SEF should be especially vigilant regarding potential conflicts of interest when appointing a CCO.

3. Summary of Comments

WMBAA supports the proposed amendments to § 37.1501(b) and (c). According to WMBAA, the Commission's revised rules should eliminate duplicative or unnecessary requirements, streamline existing provisions, and thereby allow SEFs to meet their statutory and regulatory obligations in a more effective and less burdensome manner.[160]

4. Final Rules and Acceptable Practice

The Commission is adopting the amendments to § 37.1501(b) and (c) as proposed. These changes will mitigate potential confusion by removing requirements that are duplicative of provisions in Core Principle 15 and references to governance structures, such as the ROC, that are not required by statute or regulation. The Commission believes the amendments granting the SEF's senior officer additional oversight authority over the CCO better reflects the reality that the senior officer is often

[159] 83 FR 62033.

[160] 2019 WMBAA Letter at 24.

better-positioned than the board of directors to facilitate a CCO's effectiveness on a day-to-day basis, while still maintaining the CCO's independence to an appropriate degree.

Further, the acceptable practice on qualifications of a CCO will provide SEFs with additional clarity on appropriate considerations in selecting a CCO, without limiting permissible considerations to the enumerated list. As stated in the acceptable practice, the Commission continues to stress the importance of considering potential conflicts of interest in appointing a CCO.

D. § 37.1501(c)—Duties of Chief Compliance Officer[161]

Existing § 37.1501(d)—"Duties of chief compliance officer"— requires a CCO, at a minimum, to: (i) oversee and review the SEF's compliance with the Act and Commission regulations;[162] (ii) resolve any conflicts of interest that may arise, including in certain enumerated circumstances;[163] (iii) establish and administer written policies and procedures reasonably designed to prevent violations of the Act and Commission regulations;[164] (iv) take reasonable steps to ensure compliance with the Act and Commission regulations;[165] (v) establish procedures for the remediation of noncompliance issues identified by the CCO through certain specified protocols;[166] (vi) establish and follow appropriate procedures for the handling, management response,

[161] The Commission is renumbering existing § 37.1501(d) to § 37.1501(c).

[162] 17 CFR 37.1501(d)(1).

[163] 17 CFR 37.1501(d)(2). A CCO is specifically required to address conflicts between (i) business considerations and compliance requirements; (ii) business considerations and the requirement that the SEF provide fair, open, and impartial access under § 37.202; and (iii) a SEF's management and board members. 17 CFR 37.1501(d)(2)(i) through (iii).

[164] 17 CFR 37.1501(d)(3).

[165] 17 CFR 37.1501(d)(4).

[166] 17 CFR 37.1501(d)(5).

remediation, retesting, and closing of noncompliance issues;[167] (vii) establish and administer a compliance manual and a written code of ethics;[168] (viii) supervise a SEF's self-regulatory program;[169] and (ix) supervise the effectiveness and sufficiency of any regulatory services provided to the SEF in accordance with § 37.204.[170]

1. Proposed Rules

The Commission proposed to consolidate certain existing provisions of § 37.1501(d) (to be renumbered as § 37.1501(c)), specify a CCO may identify noncompliance matters through "any means" in addition to the currently prescribed means, and clarify that the procedures followed to address noncompliance issues must be "reasonably designed" by the CCO to handle, respond, remediate, retest, and resolve noncompliance issues identified by the CCO.[171] The Proposed Rules acknowledged that a CCO may not be able to design procedures that detect all possible noncompliance issues and noted that a CCO may utilize a variety of resources to identify noncompliance issues beyond a limited set of means.

The Commission also proposed to amend the CCO's duty to resolve conflicts of interest.[172] First, the CCO would be required to take "reasonable steps" to resolve

[167] 17 CFR 37.1501(d)(6).

[168] 17 CFR 37.1501(d)(7).

[169] 17 CFR 37.1501(d)(8).

[170] 17 CFR 37.1501(d)(9).

[171] Existing paragraph § 37.1501(d)(5) requires a CCO to establish procedures for remediation of noncompliance issues identified through a compliance office review, look-back, internal or external audit finding, self-reported error, or validated complaint. Existing paragraph § 37.1501(d)(6) requires a CCO to establish and follow appropriate procedures for the handling, management response, remediation, retesting, and closing of noncompliance issues. The Commission proposed to consolidate and amend these requirements, and renumber the consolidated requirement to paragraph § 37.1501(c)(5).

[172] The Commission proposed to renumber existing § 37.1501(d)(2), which addresses the CCO's duty to resolve conflicts of interest, to § 37.1501(c)(2) and amend the requirement as described.

"material" conflicts of interest that may arise.[173] This proposed amendment reflects the Commission's view that the current requirement is overly broad and impractical because a CCO cannot be reasonably expected to successfully resolve every potential conflict of interest that may arise. The Commission further proposed to eliminate the existing enumerated conflicts of interest to avoid any inference that they are an exhaustive list of conflicts that a CCO must address.[174]

The Commission stated these proposed amendments would not weaken the CCO's statutory duty to address conflicts of interest, but rather reflect the CCO's practical ability to detect and resolve conflicts.[175] Moreover, the proposed amendments reflected the Commission's belief that a CCO should have discretion to determine the conflicts that are material to the SEF's ability to comply with the Act and the Commission's regulations.[176]

2. Summary of Comments

WMBAA supports the proposed changes to the CCO's duties.[177]

3. Final Rules

The amendments are being finalized as proposed, with one exception. The Commission notes the list of potential conflicts that a CCO should resolve under existing

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[173] The Commission also proposed to eliminate "a body performing a function similar to the board of directors" under proposed § 37.1501(c)(2) (existing § 37.1501(d)(2)), as this phrase is already included in the definition of "board of directors" under § 37.1501(a).

[174] These provisions are currently set forth under existing § 37.1501(d)(2)(i) through (iii). The Commission also proposed additional, technical changes to existing § 37.1501(d), (d)(1), d(7) and d(8), to renumber them as § 37.1501(c), (c)(1), (c)(6) and (c)(7), respectively and to renumber existing paragraph § 37.1501(c)(9) as § 37.1501(c)(8).

[175] 84 FR 62034.

[176] *Id.*

[177] 2019 WMBAA Letter at 25.

§ 37.1500(d)(2) does not create an inference that they are an exhaustive list of conflicts that a CCO must address but, instead, provides useful examples, and the list will not be eliminated as proposed.[178] The Commission continues to believe the amendments do not weaken the CCO's duties to identify and address conflicts of interest. Rather, the amendments reflect the practical reality that, in the Commission's experience, a CCO cannot be reasonably expected to successfully detect and resolve every potential conflict of interest that may arise.

E. § 37.1501(d)—Preparation of Annual Compliance Report[179]

Existing § 37.1501(e)—"Preparation of annual compliance report"—requires the CCO to annually prepare and sign an ACR that, at a minimum, (i) describes the SEF's written policies and procedures, including the code of ethics and conflicts of interest policies;[180] (ii) reviews the SEF's compliance with the Act and Commission regulations in conjunction with the SEF's policies and procedures;[181] (iii) provides a self-assessment of the effectiveness of the SEF's policies and procedures, including areas of improvement and related recommendations for the SEF's compliance program or resources;[182] (iv) lists material changes to the policies and procedures;[183] (v) describes the SEF's financial, managerial, and operational resources, including compliance program staffing and resources, a catalogue of investigations and disciplinary actions, and a review of the

[178] The list will be re-designated as § 37.1501(c)(2)(i) through (iv).

[179] The Commission is renumbering existing § 37.1501(e) to § 37.1501(d).

[180] 17 CFR 37.1501(e)(1).

[181] 17 CFR 37.1501(e)(2)(i).

[182] 17 CFR 37.1501(e)(2)(ii) through (iii).

[183] 17 CFR 37.1501(e)(3).

disciplinary committee's performance;[184] (vi) describes any material compliance matters identified through certain enumerated mechanisms (*e.g.*, compliance office review or lookback), and explains how they were resolved;[185] and (vii) certifies that, to the best of the CCO's knowledge and reasonable belief and under penalty of law, the ACR report is accurate and complete.[186]

After part 37 was implemented, the Commission gained experience and received feedback on the ACR requirements. The Commission determined that some of the required ACR content provides it with minimal meaningful insight into a SEF's compliance program. For example, some of the content is duplicative of information obtained by the Commission from other reporting channels, such as the system-related information that a SEF must file pursuant to Core Principle 14 and rule certifications filed pursuant to part 40 of the Commission's regulations.[187] Various SEF CCOs also have provided feedback that certain ACR content requires substantial time to prepare and includes some information that does not change frequently.[188] SEFs requested that the Commission simplify those requirements and provide additional time to file the reports. To this end, the Commission notes many SEFs have not provided sufficient assessments whether their respective policies and procedures (*e.g.*, rulebooks, compliance manuals,

[184] 17 CFR 37.1501(e)(4).

[185] 17 CFR 37.1501(e)(5).

[186] 17 CFR 37.1501(e)(6).

[187] Among other information required to be submitted to the Commission pursuant to part 40, a SEF is required to provide the Commission with amendments to its rulebook and compliance manual.

[188] *See* CFTC Staff Letter No. 17-61 (citing testimonials from SEFs that the preparation of an ACR requires an extensive information-gathering process, including review and documentation of information gathered on an entity-wide basis).

conflict of interest policies, codes of ethics, governance documentation, and third-party service agreements) comply with the Act and Commission regulations.

1. Proposed Rules

Based upon its experience in reviewing ACRs, the Commission proposed certain amendments to eliminate duplicative or unnecessary information requirements and streamline existing requirements, thereby reducing unnecessary regulatory burdens and compliance costs associated with certain aspects of ACRs. The Commission also proposed certain amendments to enhance the usefulness of ACRs by enabling the Commission to better assess the effectiveness of a SEF's compliance and self-regulatory programs.

Under the proposed approach, a SEF would no longer need to include in its ACR either a review of all the Commission regulations applicable to a SEF or an identification of the written policies and procedures designed to ensure compliance with the Act and Commission regulations.[189] Instead, under proposed § 1501(d)(1), a SEF would be required to include in the ACR a description and self-assessment of the effectiveness of the SEF's written policies and procedures to "reasonably ensure" compliance with the Act and applicable Commission regulations. The Commission stated its belief that this approach is more closely aligned with the corresponding provisions of Core Principle 15 and would still allow the Commission to properly assess the SEF's compliance and self-regulatory programs.[190] Similarly, the Commission also proposed to eliminate a required

[189] The Commission proposed to eliminate these requirements in the introductory language of existing § 1501(e)(2) and § 1501(e)(2)(i).

[190] 83 FR 62035. As proposed, a SEF would continue to be required to describe the SEF's written policies and procedures, consistent with Core Principle 15. In addition to the required description, the Commission proposed to consolidate and amend existing § 37.1501(e)(2)(ii), which requires a SEF to provide in the

discussion of the SEF's compliance staffing and structure; a catalogue of investigations and disciplinary actions taken over the last year; and a review of disciplinary committee and panel performance.[191] A SEF would continue to be required to describe in its ACR the SEF's financial, managerial, and operational resources set aside for compliance.[192] By refining the scope of information a SEF would be required to include in its ACR, the Commission intended to allow SEFs to devote their resources to providing more detailed—and ultimately better-quality—information that will better facilitate assessments of compliance.

To enhance the Commission's ability to assess a SEF's written policies and procedures regarding compliance matters, the Commission also proposed to require a SEF to discuss only material noncompliance matters and explain the corresponding actions taken to resolve such matters.[193] The Commission stated requiring SEFs to focus on describing material noncompliance matters, rather than describing *all* compliance matters in similar depth, would streamline this requirement and provide more useful information to the Commission.[194] Further, the Commission proposed to eliminate the

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ACR a self-assessment as to the effectiveness of its policies and procedures, with existing § 37.1501(e)(1), and renumber the consolidated requirement to § 37.1501(d)(1). Further, the Commission proposed to consolidate and amend existing § 37.1501(e)(2)(iii), which requires an ACR to discuss areas for improvement and recommend potential or prospective changes or improvements to a SEF's compliance program and resources, with existing § 37.1501(e)(3) and renumber the consolidated requirement to § 37.1501(d)(2). The Commission expects the CCO will provide more nuanced and in-depth discussions through these consolidated provisions, rather than merely providing generalized responses.

[191] The Commission proposed to eliminate these requirements under existing § 37.1501(e)(4).

[192] The Commission proposed to renumber the remaining requirements under existing § 37.1501(e)(4) to § 37.1501(d)(3) and adopt technical amendments.

[193] The Commission proposed to renumber this requirement under existing § 37.1501(e)(5) to § 37.1501(d)(4) and adopt the amendments as described above and additional, technical changes.

[194] 83 FR 62035.

enumerated mechanisms for identifying noncompliance issues, conforming to the ability of a CCO to establish procedures to identify noncompliance issues through "any means," as described above.[195]

Consistent with these proposed amendments, the Commission also proposed to limit a SEF CCO's certification of an ACR's accuracy and completeness to "all material respects" of the report.[196] The Commission recognized CCOs have been hesitant to certify that an entire ACR is accurate and complete under the penalty of the law, without regard to whether a potential inaccuracy or omission would be a material error or not. The Commission believed the proposed change would appropriately address SEF CCOs' concerns regarding potential liability while ensuring the material accuracy of an ACR submitted to the Commission.[197]

2. Summary of Comments

Refinitiv and WMBAA support the proposed amendments to the preparation of the ACR.[198] Refinitiv believes the ACR is unduly burdensome to prepare in its current form in comparison to the regulatory benefits of much of the information required to be provided; and the proposed amendments would more closely harmonize a SEF's ACR requirements with ACR requirements for a swap dealers or futures commission merchants. Refinitiv supports the proposal to eliminate the requirement to include a chart identifying a specific policy or procedure reasonably designed to ensure compliance with

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[195] *See* Section IV.D., *supra*. The Commission proposed to eliminate these enumerated mechanisms from the ACR requirements under existing paragraph (e)(5).

[196] The Commission proposed to renumber existing § 37.1501(e)(6) to § 37.1501(d)(5) and amend the requirement as described.

[197] 83 FR 62035.

[198] 2019 WMBAA Letter at 25-26; Refinitiv Letter at 14.

each individual regulation and paragraph of a regulation. In Refinitiv's view, the proposed requirements regarding CCO reports would ensure a proper compliance review on an annual basis without the unnecessary costs incurred in connection with producing such a chart.

3. Final Rules

The Commission is adopting the amended requirements for preparation of an ACR as proposed. The streamlined content requirements will allow SEF CCOs to focus on providing complete and accurate information on the compliance matters that are most critical to the Commission's oversight of SEFs, and allow the Commission to conduct a more efficient and effective review of an ACR and assessment of a SEF's compliance.

F. § 37.1501(e)—Submission of Annual Compliance Report and Related Matters[199]

Existing § 37.1501(f)(1) requires a CCO to provide the ACR to the board or, in the absence of a board, the senior officer for review.[200] The board of directors and senior officer may not require the CCO to change the ACR.[201] The SEF's board minutes, or a similar written record, must reflect the submission of the ACR to the board of directors or senior officer and any subsequent discussion of the report.[202] Additionally, the SEF must concurrently file the ACR and the fourth-quarter financial statements with the Commission within 60 calendar days of the end of the SEF's fiscal year end.[203] The CCO must certify and promptly file an amended ACR with the Commission upon the

[199] The Commission is renumbering existing § 37.1501(f) to § 37.1501(e).

[200] 17 CFR 37.1501(f)(1).

[201] *Id.*

[202] *Id.*

[203] 17 CFR 37.1501(f)(2).

discovery of any material error or omission in the report.[204] A SEF may request an extension of the ACR filing deadline based on substantial, undue hardship in filing the ACR on time.[205]

1. Proposed Rules

The Commission proposed several amendments to the ACR submission procedures. First, the Commission proposed to provide SEFs with an additional 30 days to file the ACR with the Commission, but no later than 90 calendar days after a SEF's fiscal year end.[206] The Commission recognized that in addition to the ACR, SEFs have other reporting obligations, such as the fourth-quarter financial report required to be submitted under Core Principle 13 and other year-end reports; and SEFs have indicated that these multiple reporting obligations present resource constraints on SEFs and their CCOs.[207] In addition to an extended deadline, the Commission proposed to replace the "substantial and undue hardship" standard required for filing ACR extensions with a "reasonable and valid" standard.[208] Further, the Commission proposed to eliminate the requirement that each SEF must document the submission of the ACR to the SEF's board of directors or senior officer in board minutes or some other similar written record,[209] noting that the Core Principle 15 recordkeeping requirement under proposed §

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[204] 17 CFR 37.1501(f)(3).

[205] 17 CFR 37.1501(f)(4).

[206] The Commission proposed to renumber existing § 37.1501(f)(2) to § 37.1501(e)(2), amend the requirement as described, and adopt additional, technical amendments to the existing language. The Commission also proposed to add a title to this paragraph—"Submission of annual compliance report to the Commission."

[207] 83 FR 62036.

[208] The Commission proposed to renumber existing § 37.1501(f)(4) to § 37.1501(e)(4) and amend the provision as described. The Commission also proposed to add a title—"Request for extension."

[209] The Commission proposed to eliminate this requirement under existing paragraph (f)(1).

37.1501(f), discussed below, would incorporate this requirement.[210] The Commission also proposed to require the CCO to submit an amended ACR to the SEF's board of directors—or, in the absence of a board of directors, the senior officer of the SEF—for review prior to submitting the amended ACR to the Commission; this approach is the same as the requirements that exist for submitting an initial ACR.[211]

2. Summary of Comments

WMBAA supports the proposed amendments to the ACR submission requirements.[212]

3. Final Rules

The amendments to the ACR submission requirements are being finalized as proposed. Given other relevant end-of-year reporting requirements, including the SEF's required fourth-quarter financial report (as well as any reporting required of the SEF's affiliates under other regulatory regimes), the Commission continues to believe a 30-day extension of the submission timeline and a less stringent "reasonable and valid" standard for further extensions will facilitate more accurate and useful reporting to the

[210] Existing § 37.1501(g) sets forth recordkeeping requirements for SEFs related to the CCO's duties. As discussed below, the Commission is amending those requirements.

[211] The Commission proposed to renumber existing § 37.1501(f)(3) to § 37.1501(e)(3) and add a title—"Amendments to annual compliance report." The Commission proposed to adopt this requirement under § 37.1501(e)(3)(i). Under proposed § 37.1501(e)(3)(ii), an amended ACR would be subject to the amended certification requirement, *i.e.*, a CCO must certify that the ACR is accurate and complete in all material respects. The Commission also proposed to renumber existing § 37.1501(f) to § 37.1501(e) and change the title to "Submission of annual compliance report and related matters." The Commission also proposed to renumber existing § 37.1501(f)(1) to § 37.1501(e)(1), adopt additional, technical amendments to the existing language, and add a title—"Furnishing the annual compliance report prior to submission to the Commission."

[212] 2019 WMBAA Letter at 27.

Commission.[213] The additional requirements for board of directors or senior officer review of an amended ACR will likewise foster increased accuracy and precision in regulatory reporting.

G. § 37.1501(f)—Recordkeeping[214]

Existing § 37.1501(g)(1) requires a SEF to maintain a copy of written policies and procedures adopted in furtherance of compliance with the Act and the Commission's regulations;[215] copies of all materials created in furtherance of the CCO's duties under existing § 37.1501(d)(8) and (9);[216] copies of all materials in connection with the review and submission of the ACR;[217] and any records relevant to the ACR.[218] Existing § 37.1501(g)(2) requires the SEF to maintain these records in accordance with § 1.31 and part 45 of the Commission's regulations.[219]

1. Proposed Rules

The Commission proposed to streamline the recordkeeping requirements that pertain to the CCO's duties and the preparation and submission of the ACR. Specifically, the Commission proposed to revise § 37.1501(f) to require a SEF to keep all records demonstrating compliance with the duties of the CCO and the preparation and submission

[213] A SEF requesting an extension must identify the circumstances creating a reasonable and valid need for the extension. The Commission—and, when exercising the delegated authority discussed below, the Director of the Division of Market Oversight—reserves the discretion to determine that the rationale proffered by the SEF is not objectively reasonable and valid.

[214] The Commission is renumbering existing paragraph (g) to paragraph (f).

[215] 17 CFR 37.1501(g)(1)(i).

[216] 17 CFR 37.1501(g)(1)(ii).

[217] 17 CFR 37.1501(g)(1)(iii).

[218] 17 CFR 37.1501(g)(1)(iv).

[219] 17 CFR 37.1501(g)(2).

of the ACR consistent with the recordkeeping requirements under §§ 37.1000 and 37.1001.[220]

2. Summary of Comments

The Commission did not receive any comments on the proposed amendments to the CCO's recordkeeping requirements.

3. Final Rules

The Commission is adopting the recordkeeping requirements as proposed. The Commission believes the simplified requirements will better ensure access to relevant compliance information.

H. § 37.1501(g)—Delegation of Authority[221]

Existing § 37.1501(h)—"Delegation of authority"—delegates the authority to grant or deny a SEF's request for an extension of time to file its ACR to the Director of DMO.[222] In addition to renumbering this provision based on the amendments described above, the Commission proposed to adopt additional, technical amendments that conform to the proposed amendments to the Core Principle 15 regulations discussed above. The Commission received no comments on the proposal and is adopting the amendments as proposed.

[220] 17 CFR 37.1501(f); 17 CFR 37.1000 and 37.1001.

[221] The Commission is renumbering existing § 37.1501(h) to § 37.1501(g).

[222] 17 CFR 37.1501(h).

V. Related Matters

A. Regulatory Flexibility Act

The Regulatory Flexibility Act ("RFA") requires federal agencies, in promulgating rules, to consider the impact of those rules on small entities.[223] The Commission has previously established certain definitions of "small entities" to be used by the Commission in evaluating the impact of its rules on small entities in accordance with the RFA.[224] The changes to part 37 adopted herein would have a direct effect on the operations of SEFs. The Commission has previously certified that SEFs[225] are not small entities for purpose of the RFA. Accordingly, the Commission does not believe the Final Rules will have a significant economic impact on a substantial number of small entities. Therefore, the Chairman, on behalf of the Commission, pursuant to 5 U.S.C. 605(b), hereby certifies that the Final Rules will not have a significant economic impact on a substantial number of small entities.

B. Paperwork Reduction Act

1. Background

The Paperwork Reduction Act of 1995 ("PRA")[226] imposes certain requirements on Federal agencies (including the Commission) in connection with their conducting or sponsoring a collection of information as defined by the PRA. An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information

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[223] *See* 5 U.S.C. 601 et seq.

[224] *See* Policy Statement and Establishment of "Small Entities" for purposes of the Regulatory Flexibility Act, 47 FR 18618 (Apr. 30, 1982).

[225] Core Principles and Other Requirements for Swap Execution Facilities, 78 FR 33476, 33548 (June 4, 2013).

[226] 44 U.S.C. 3501 et seq.

unless it displays a currently valid control number issued by the Office of Management and Budget ("OMB").

The rule amendments adopted herein will result in the revision of a collection of information for which the Commission has previously received a control number from OMB: OMB Control Number 3038-0074, Core Principles and Other Requirements for Swap Execution Facilities. The responses to this collection of information are mandatory.

The Commission did not receive any comments regarding its PRA burden analysis in the preamble to the notice of proposed rulemaking. The Commission is revising information collection number 3038-0074 to reflect the adoption of amendments to part 37 of its regulations, as discussed below, but does not believe the regulations as adopted impose any other new collections of information that require approval of OMB under the PRA.

2. New Information Collection Requirements and Related Burden Estimates.[227]

Currently, there are approximately 19 SEFs registered with the Commission that may be impacted by this rulemaking and, in particular, the collection of information contained herein and discussed below.

i. Audit Trail Requirements Related to Post-Execution Allocation Information

Existing § 37.205(a) requires a SEF to capture and retain all audit trail data necessary to detect, investigate, and prevent customer and market abuses. Existing § 37.205(b)(2)(iv) requires a SEF's audit trail program to include an electronic transaction

[227] This discussion does not include information collection requirements that are included under other Commission regulations and related OMB control numbers. Specifically, the discussion does not include OMB control number 3038-0052, which covers, among other things, information collections arising in part 38 (other than the information collections related to § 38.12) or OMB control number 3038-0099, which covers the information collections related to the "available to trade" determination (MAT determination) process under §§ 37.10 and 38.12.

history database that identifies, among other things, each account to which order fills are allocated. The Commission proposed to eliminate the requirements in § 37.205(a) and (b)(2)(iv) that a SEF capture post-execution allocation information in its audit trail. Instead, the Commission proposed to require that SEFs capture in their audit trail information only through execution on the SEF. The Commission is adopting the amendments as proposed.

As noted in the Proposed Rules, to the extent that the Commission is providing SEFs with greater discretion in fulfilling their information collection obligations with respect to audit trail requirements under § 37.205, the Commission estimates and assumes SEFs will continue to fulfill their information collection burdens in a manner similar to the status quo. Accordingly, amended § 37.205(a) and (b) will not substantively or materially affect a SEF's total information collection burden hours. With respect to § 37.205(a), the Commission's proposal to eliminate such information collections will not result in a net change to a SEF's aggregate burden hours because the 2016 Part 37 PRA Renewal already considered such relief and non-compliance with such requirements in its revised estimate.

ii. Financial Resources Requirements

Core Principle 13 requires a SEF to have adequate financial, operational, and managerial resources to discharge its responsibilities. To achieve financial resource adequacy, a SEF must maintain financial resources sufficient to cover its operating costs for a period of at least one year, calculated on a rolling basis. The Commission implemented Core Principle 13 by adopting §§ 37.1301 through 37.1307 to specify: (i) the eligible types of financial resources that may be counted toward compliance (§

37.1302); (ii) the computation of projected operating costs (§ 37.1303); (iii) valuation requirements (§ 37.1304); (iv) a liquidity requirement for those financial resources that is equal to six months of a SEF's operating costs (§ 37.1305); and (v) reporting obligations (§ 37.1306). These regulations are intended to ensure that a SEF has financial strength sufficient to discharge its responsibilities, maintain market continuity, and withstand unpredictable market events.

The Commission proposed several amendments to the Core Principle 13 regulations to achieve a better balance between ensuring SEF financial stability, promoting SEF growth and innovation, and reducing unnecessary costs. The proposed rules: (i) clarify the scope of operating costs that a SEF must cover with adequate financial resources; (ii) set forth acceptable practices, based on existing Commission staff guidance, that address the discretion that a SEF has when calculating projected operating costs pursuant to proposed § 37.1304; (iii) amend the existing six-month liquidity requirement for financial resources held by a SEF; and (iv) streamline requirements with respect to financial reports filed with the Commission. The Commission also proposed amendments to clarify certain existing requirements, including the renumbering of several provisions to present the requirements in a more cohesive manner.

The Commission is adopting the amendments to §§ 37.1301 through 37.1307 as proposed. With respect to two questions posed in the notice of proposed rulemaking, the Commission will not adopt the requirement that financial statements be audited, and the Commission will retain the existing quarterly reporting requirement for SEFs, rather than moving to a semiannual reporting requirement.

As stated in the notice of proposed rulemaking, the Commission estimates the amendment to § 37.1301(b) will decrease the annual recurring information collection burden hours by five burden hours; the amendment to § 37.1306 will increase the annual recurring information collection burden hours by 10 burden hours and not impose an initial, non-recurring burden; and the amendment to § 37.1306(c) will impose an initial, non-recurring information collection of 20 burden hours and five annual recurring information collection burden hours after the initial year to update the information. Other than as discussed above, the Commission believes the amendment to § 37.1306(c) will not impose new information collection burdens on SEFs or substantively or materially modify existing burdens.

iii. Chief Compliance Officer Requirements

Statutory Core Principle 15 requires each SEF to designate a CCO and sets forth its corresponding duties. Among other responsibilities, the CCO is required to ensure the SEF complies with the CEA and applicable rules and regulations, and to establish and administer required policies and procedures. Core Principle 15 also requires the CCO to prepare and file an ACR to the Commission. The Commission promulgated requirements under § 37.1501 to implement these requirements.

The Commission proposed several amendments to § 37.1501 based on the Commission's experience since the part 37 implementation. These amendments streamline CCO requirements; allow SEF management to exercise discretion in CCO oversight; and simplify the preparation and submission of the ACR. Specifically, the proposed changes: (i) add the definition of "senior officer;" (ii) eliminate the existing ROC-related requirements; (iii) allow the SEF's senior officer to have the same oversight

responsibilities over the CCO as the board; (iv) eliminate the limitations on authority to remove the CCO, which currently restricts that removal authority to a majority of the board, or in the absence of a board, the senior officer; (v) add a new acceptable practice to Core Principle 15 in Appendix B associated with § 37.1501(b)(2)(i), which requires the CCO to have the background and skills appropriate to the position and states that a SEF should be especially vigilant regarding potential conflicts of interest when appointing the CCO; (vi) adopt several amendments to clarify and streamline the CCO's duties, including refining the scope of the CCO's duty to taking only "reasonable steps" to resolve "material" conflicts of interest that may arise; and (vii) make other amendments, including elimination of duplicative rules and renumbering and consolidation of existing provisions. The amendments are being finalized as proposed, with one exception. The Commission is not eliminating the list of potential conflicts that the CCO should resolve under existing § 37.1501(d)(2).

With respect to the ACR, existing § 37.1501(e) requires the CCO to prepare and sign annually an ACR that, at a minimum: (i) describes the SEF's written policies and procedures; (ii) reviews the SEF's compliance with the Act and Commission regulations; (iii) provides a self-assessment of the effectiveness of the SEF's policies and procedures; (iv) lists material changes to the policies and procedures; (v) describes the SEF's financial, managerial, and operational resources; (vi) describes any material compliance matters identified through certain enumerated mechanisms and explains how they were resolved; and (vii) certifies that, to the best of the CCO's knowledge and reasonable belief and under penalty of law, the ACR is accurate and complete.

The Commission proposed several amendments to simplify the ACR submission procedures including: providing SEFs with an additional 30 days to file the ACR with the Commission, but no later than 90 calendar days after a SEF's fiscal year end, and requiring the CCO to submit an amended ACR to the SEF's board or, in the absence of a board, the senior officer of the SEF, for review prior to submitting the amended ACR to the Commission. The proposed rules also would streamline the recordkeeping requirements that pertain to the CCO's duties and the preparation and submission of the ACR. The amendments to the ACR preparation, submission and recordkeeping requirements are being adopted and finalized as proposed.

As stated in the notice of proposed rulemaking, the Commission estimates the amendment to § 37.1501(d) will reduce annual recurring information collection burden hours by approximately 10 burden hours per SEF. The amendment to § 37.1501(d)(3) will reduce annual recurring information collection burden hours by approximately five burden hours per SEF. The amendment to § 37.1501(d)(4) will reduce annual recurring information collection burden hours per SEF by three burden hours. The amendment to § 37.1501(d)(5) will reduce annual recurring information collection burden hours per SEF/CCO by 10 burden hours.

C. Cost-Benefit Considerations

1. Introduction

Section 15(a) of the CEA requires the Commission to consider the costs and benefits of its actions before promulgating a regulation under the CEA or issuing certain orders.[228] Section 15(a) further specifies that the costs and benefits shall be evaluated in

[228] 7 U.S.C. 19(a).

light of the following five broad areas of market and public concern: (i) protection of market participants and the public; (ii) efficiency, competitiveness, and financial integrity of futures markets; (iii) price discovery; (iv) sound risk management practices; and (v) other public interest considerations.

2. Background

The Commission is finalizing several of the Proposed Rules. First, the Final Rules eliminate the requirement that a SEF capture post-execution allocation information in its audit trail data. Second, regarding financial resources, the Final Rules finalize amendments to the existing six-month liquidity requirement and add new acceptable practices that provide further guidance to SEFs for making a reasonable calculation of their projected operating costs. Finally, the Final Rules streamline requirements for the CCO position; allow SEF management to exercise discretion in CCO oversight; and simplify the preparation and submission of the required ACR.

The baseline against which the Commission considers the costs and benefits of the Final Rules is the statutory and regulatory requirements of the CEA and Commission regulations now in effect, in particular CEA section 2(h)(8) and certain rules in part 37 of the Commission's regulations. The Commission, however, notes that as a practical matter, SEFs have adopted some current practices included in the Final Rules based upon no-action relief and guidance provided by Commission staff that is time-limited in nature.[229] As such, to the extent that SEFs and market participants have relied on relevant

[229] CFTC Staff Letter No. 17-54 (post-execution allocation data); CFTC Staff Letter No. 17-61 (timing of the ACR submission).

Commission staff no-action relief or Commission staff guidance, the actual costs and benefits of the Final Rules may not be as significant.

In some instances, it is not reasonably feasible to quantify the costs and benefits with respect to certain factors, for example, price discovery or market integrity. Notwithstanding these limitations, however, the Commission otherwise identifies and considers the costs and benefits of these rules in qualitative terms. The Commission did not receive any comments from commenters which quantified or attempted to quantify the costs and benefits of these rules.

The following consideration of costs and benefits is organized according to the rules and rule amendments finalized in this rulemaking. For each rule, the Commission summarizes the Final Rules, and identifies and discusses the costs and benefits attributable to each rule. The Commission, where applicable, then considers the costs and benefits of the Final Rules in light of the five public interest considerations set out in section 15(a) of the CEA.

The Commission notes that this consideration of costs and benefits is based on the understanding that the swaps market functions internationally, with many transactions involving U.S. firms taking place across international boundaries, with some Commission registrants being organized outside of the U.S., with leading industry members typically conducting operations both within and outside the U.S., and with industry members commonly following substantially similar business practices wherever located. Where the Commission does not specifically refer to matters of location, the discussion of costs and benefits below refers to the effects of the Final Rules on all swaps activity subject to the final new and amended regulations, whether by virtue of the activity's physical location

in the U.S. or by virtue of the activity's connection with activities in, or effect on, U.S. commerce under CEA section 2(i).[230]

3. Audit Trail

i. Overview

Existing § 37.205(a) requires a SEF to capture and retain all audit trail data necessary to detect, investigate and prevent customer and market abuses.[231] This audit trail data must permit a SEF to track a customer order from the time of receipt through fill, allocation, or other disposition.[232] Existing § 37.205(b)(2)(iv) requires a SEF's audit trail program to include an electronic transaction history database that identifies, among other things, each account to which order fills are allocated.[233]

Recognizing the practical difficulties that SEFs face in obtaining information regarding allocations that occur away from the SEF after a trade has been executed, the Commission is eliminating the requirements in § 37.205(a) and (b)(2)(iv) that a SEF capture post-execution allocation information in its audit trail.[234] Instead, the Final Rules require a SEF to capture in its audit trail information only through execution on the

[230] Section 2(i)(1) applies the swaps provisions of both the Dodd-Frank Act and Commission regulations promulgated under those provisions to activities outside the United States that have a direct and significant connection with activities in, or effect on, commerce of the United States. 7 U.S.C. 2(i). Section 2(i)(2) makes them applicable to activities outside the United States that contravene Commission rules promulgated to prevent evasion of the Dodd-Frank Act.

[231] 17 CFR 37.205(a). Such audit trail data must be sufficient to reconstruct all indications of interest, RFQs, orders, and trades.

[232] *Id.*

[233] 17 CFR 37.205(b)(2)(iv).

[234] 83 FR at 62005.

SEF.[235] The Commission has noted that this change would be consistent with current swap market practice.[236]

ii. Benefits

Post-execution allocations are made away from SEFs and typically occur between the clearing firm or the customer and the DCO, or at the middleware provider.[237] In general, SEFs do not have access to post-execution allocation information and are unable to obtain such data from third parties, such as DCOs and swap data repositories, due to confidentiality concerns. Commission staff has issued no-action relief from this requirement.[238] This rulemaking creates regulatory certainty by codifying the no-action relief, which will permit SEFs to maintain their existing practice and avoid any legal exposure due to a SEF's inability to comply with regulations.

iii. Costs

The changes to the existing audit trail requirements may reduce the scope of information captured in a SEF's audit trail, but the Commission believes that these changes are not likely to affect materially the protection of market participants and the public. The Commission notes that post-execution allocation information has generally not been captured because SEFs have operated under no-action relief, which was provided by Commission staff due to the general inability of SEFs to access this

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[235] *Id.*

[236] *Id.*

[237] CFTC Staff Letter No. 17-54. SEFs have noted that even if they could obtain the information from DCOs, swap data repositories, or middleware providers, or alternatively, from the counterparties to the swap, the infrastructure necessary to securely transmit the post-execution allocation information, such as an application-programming interface or secure file transfer protocol site, is currently not in place.

[238] *Id.*

information. Thus, although the elimination of the requirement to capture and retain post-execution allocation information is a regulatory change, it should not have a material effect on the status quo.

iv. Section 15(a) Factors

(1) Protection of Market Participants and the Public

The Commission believes the revised audit trail requirements provide a nearly identical level of protection to market participants and the public as provided under the existing rules. As noted above, SEFs generally do not capture post-execution allocation information in their audit trail because SEFs have operated under no-action relief, which was provided by Commission staff due to the general inability of SEFs to access this information. Moreover, the Commission is able to obtain post-execution allocation information from other registered entities and is not aware that SEFs' reliance on the relief from collecting post-execution allocation information has raised any regulatory concerns. Thus, elimination of the requirement that SEFs capture and retain post-execution allocation information should not have a material effect on the level of protection for market participants and the public relative to the status quo, although it is a regulatory change.

(2) Efficiency, Competitiveness, and Financial Integrity of the Markets

The Commission believes that there will be no substantive change to the efficiency, competitiveness, and financial integrity of markets because SEFs will continue to capture information through execution in the audit trail and the Commission has the ability to obtain post-execution allocation information from other registrants.

Further, the amendments to § 37.205 will not change the current status quo in the markets.

(3) Price Discovery

The Commission believes these rules will have no effect on price discovery because they affect only how SEFs track and audit trades and do not change what information is disclosed to market participants. Further, the amendments to § 37.205 will not change the current status quo in the markets.

(4) Sound Risk Management Practices

The Commission believes these rules will have no material effect on sound risk management practices because they do not change the status quo and the Commission is not aware that SEFs' reliance on the no-action relief from collecting post-execution allocation information has raised any regulatory concerns.

(5) Other Public Interest Considerations

The Commission has not identified any effects that these rules will have on public interest considerations other than those enumerated above, nor did any commenter suggest one.

v. Consideration of Alternatives and Comments

Commenters support the proposal to eliminate the requirement to capture and retain post-execution allocation information because SEFs remain unable to obtain the

information.[239] Further, in WMBAA's view, the proposal "will [not] lead to degradation of the ability to reconstruct a trade and the environment in which it is traded."[240]

4. Financial Resources

i. Overview

The Final Rules improve on the existing rules to apply the existing Core Principle 13 financial resources requirements to SEF operations in a more practical manner, including through amendments to the existing six-month liquidity requirement and the addition of new acceptable practices that provide further guidance to SEFs for making a reasonable calculation of their projected operating costs.

Amended § 37.1301 requires a SEF to maintain financial resources in an amount adequate to cover only those projected operating costs necessary to enable the SEF to comply with its core principle obligations under section 5h of the Act and any applicable Commission regulation for a one-year period, calculated on a rolling basis.[241] In contrast, existing § 37.1301 requires a SEF to maintain sufficient financial resources to cover all of its operations for a one-year period, calculated on a rolling basis, regardless of whether such operating costs are necessary for the SEF to comply with its core principle or other applicable Commission regulations.

[239] Refinitiv Letter at 11 ("Refinitiv SEF supports the elimination of the requirement to be able to track an order through fill, allocation or other disposition, because SEFs generally do not have access to most post-execution information."); 2019 WMBAA Letter at 12-13 ("The WMBAA supports the Commission's proposal regarding audit trail requirements.").

[240] 2019 WMBAA Letter at 12-13.

[241] 37 CFR 37.1301.

Pursuant to existing § 37.1303, a SEF has reasonable discretion to determine its financial obligations under § 37.1301.[242] The Commission is adopting acceptable practices in Appendix B to Part 37 that offer guidance on the costs that a SEF may exclude in its reasonable discretion when determining its projected operating costs under § 37.1301(a). The acceptable practices are based upon financial resources guidance that was provided to the public by Commission staff and discuss the scope of a SEF's reasonable discretion for determining its obligations under §§ 37.1301 and 37.1303, as amended.

Specifically, the financial resources guidance provides that a SEF may reasonably exclude from its projected operating costs certain expenses, including: (i) costs attributable solely to sales, marketing, business development, or recruitment;[243] (ii) compensation and related taxes and benefits for SEF employees whose functions are not necessary to meet the SEF's regulatory responsibilities;[244] (iii) costs for acquiring and defending patents and trademarks for SEF products and related intellectual property; (iv) magazine, newspaper, and online periodical subscription fees; (v) tax preparation and

[242] Existing § 37.1303 provides a SEF has reasonable discretion in determining the methodology used to compute its projected operating costs in order to determine the amount needed to meet its requirements under § 37.1301. Because the liquidity requirement in existing § 37.1305 is based upon a SEF's financial requirement under § 37.1301, the SEF's application of its reasonable discretion also implicitly determines its liquidity obligation under amended § 37.1303. The Commission is adopting additional, technical changes to § 37.1302. The Commission is renumbering § 37.1304 to § 37.1305 and is not adopting substantive changes to the provision.

[243] The costs listed in this item (i) also include costs for travel, entertainment, events and conferences to the extent that such costs are not necessary to meet the SEF's regulatory responsibilities.

[244] For example, if a SEF requires a certain number of voice brokers to run its voice/hybrid platform but hires additional voice brokers to provide enhanced customer service, the SEF will need to include only the minimum number of voice brokers to run its voice/hybrid platform based on its current business volume, and taking into account any projected increase or decrease in business volume, in its projected operating cost calculations.

audit fees; (vi) to the extent not covered by item (ii) above, the variable commissions that a voice-based SEF may pay to its employee-brokers, calculated as a percentage of transaction revenue generated by the voice-based SEF; and (vii) any non-cash costs, including depreciation and amortization. The Commission similarly is incorporating this list with certain conforming changes into the acceptable practices as costs that the Commission believes may be reasonable for a SEF to exclude from its projected operating cost calculations.[245] Further, based on the financial resources guidance, the acceptable practices clarify that in order to determine its obligations under amended § 37.1301(a), a SEF may prorate, but not exclude, certain expenses in calculating projected operating costs.[246] In prorating these expenses, however, a SEF needs to document, identify, and justify its decision to prorate such expenses.

Amended § 37.1303 requires a SEF to maintain liquid assets in an amount equal to the greater of (i) three months of projected operating costs necessary to enable the SEF to comply with its core principle obligations and applicable Commission regulations, or (ii) the SEF's projected wind-down costs. In contrast, under existing rules, a SEF must maintain sufficient liquid assets to cover six months of projected operating costs. As

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[245] In order to conform to the change to § 37.1301(a), the Commission is slightly altering the wording of item (ii) to provide that a SEF may exclude the costs of a SEF's employees that are not necessary "to *comply with* the core principles set forth in section 5h of the Act and any applicable Commission regulations[.]" (emphasis added). Similarly, the financial resources guidance provides that a reasonable calculation of projected operating expenses must include all expenses necessary for a SEF "to discharge its responsibilities as a . . . SEF in compliance with the CEA, the Commission's regulations, and the . . . SEF's rulebooks," which is consistent with existing § 37.1301(a). However, in order to conform with amended § 37.1301(a), the acceptable practices instead provide that a SEF must include all expenses necessary for the SEF "to comply" with the core principles and any applicable Commission regulations.

[246] For example, a SEF will be permitted to prorate expenses that are shared with affiliates, *e.g.*, the costs of administrative staff or seconded employees that a SEF shares with affiliates. Further, a SEF is also permitted to prorate expenses that are attributable in part to activities that are not required to comply with the SEF core principles, *e.g.*, costs of a SEF's office space to the extent it also houses personnel whose costs may be excludable under items (i) or (ii).

discussed above, the Commission is adopting acceptable practices to provide further guidance on the costs that a SEF, based on its reasonable discretion, may exclude from its projected operating costs when determining its financial obligations under amended § 37.1303.

Amended § 37.1306(a) requires a SEF's quarterly financial submissions to conform to U.S. GAAP, or in the case of a non-U.S. domiciled SEF that is not otherwise required to prepare U.S. GAAP-compliant statements, to prepare its statements in accordance with either the International Financial Reporting Standards issued by the International Accounting Standards Board, or a comparable international standard that the Commission may accept in its discretion. Amended § 37.1306(c) provides that a SEF's quarterly financial statements must explicitly: (i) identify all the SEF's expenses without any exclusions; (ii) identify all expenses and corresponding amounts that the SEF excluded or prorated when it determined its projected operating costs; (iii) explain why the SEF excluded or prorated any expenses; and (iv) identify and explain all costs necessary to wind down the SEF's operations. Amended § 37.1306(d) extends the deadline for a SEF's fourth-quarter financial statement from 60 to 90 days after the end of such fiscal quarter to conform to the extended deadline for a SEF's annual compliance report. Amended § 37.1306(e) is a new rule that requires a SEF to provide notice no later than 48 hours after it knows or reasonably should know it no longer meets its financial resources obligations.

ii. Benefits

The Commission expects amended § 37.1301(a) to reduce the total financial assets that most SEFs must maintain because a SEF will only be required to maintain

sufficient resources to cover its operations necessary to comply with its core principle obligations and applicable Commission regulations, rather than all of its operating costs as is required by existing § 37.1301(a). With respect to § 37.1301(a), the acceptable practices provide further guidance regarding the scope of a SEF's reasonable discretion when determining the SEF's financial requirements under amended § 37.1301(a) to exclude certain expenses from its projected operating cost calculations, thereby reducing the amount of total financial assets that a SEF must maintain under amended § 37.1301(a). To the extent that the acceptable practices generally adopt the Commission staff's existing financial resources guidance, SEFs may already have realized the benefits associated with reduced financial resources requirements.

The liquidity requirement in amended § 37.1303 significantly reduces the amount of liquid financial assets that must be maintained by most SEFs. Currently, a SEF must maintain liquid financial assets equal to six months of projected operating costs, while amended § 37.1303 only requires most SEFs to maintain three months of projected operating costs. As a result, amended § 37.1303 is expected to reduce the liquidity requirement for most SEFs by 50 percent.[247] In addition, a SEF currently must maintain liquid assets equal to six months of operating costs even if the SEF's actual wind-down costs are greater. For certain SEFs with wind-down costs that exceed six months of operating costs, amended § 37.1303 augments market integrity for such SEFs by requiring them to maintain additional liquid assets to cover their wind-down costs, even if

[247] The Commission notes that the current liquidity requirement in existing § 37.1305, as well as amended § 37.1303, permits a SEF to acquire a "committed line of credit" to satisfy the liquidity requirement. However, the Commission notes that most SEFs satisfy this requirement through maintaining liquid assets rather than obtaining a line of credit. Accordingly, as a practical matter, the Commission expects amended § 37.1303 to reduce the amount of liquid assets that a SEF must maintain. Moreover, the Commission notes that there would be additional associated costs if a SEF were to obtain a committed line of credit.

the SEF's wind-down would exceed six months, but in no event would a SEF be permitted to maintain less than three months of operating costs.

Amended § 37.1304 provides that a SEF must make a reasonable calculation of projected wind-down costs, but has reasonable discretion in adopting the methodology for calculating such costs. The finalized acceptable practices expound upon the reasonable discretion that a SEF has for computing its projected operating costs to exclude certain expenses from its projected three months of operating cost calculations.

The Commission believes the Final Rules provide SEFs with greater flexibility in terms of establishing their financial resources. This, in turn, may lead to greater efficiencies in terms of financing and capital allocation and investment. However, the Commission acknowledges, as discussed below, this flexibility may increase the level of financial risk at the SEF.

Amended §§ 37.1306(a) and (c) will increase transparency and augment the Commission's oversight by requiring SEFs to provide standardized, U.S. GAAP-compliant financial submissions that explicitly identify any cost a SEF has excluded or prorated in determining its projected operating costs. In its experience conducting ongoing SEF oversight, Commission staff has devoted additional effort to obtain appropriate clarity and sufficient documentation from SEFs. Therefore, the Commission believes that establishing the minimum documentation that a SEF must provide will mitigate the time and resources required both by Commission staff in conducting its oversight and by SEFs in responding to Commission staff's requests for additional information. Final § 37.1306(e) benefits market integrity by ensuring that the Commission is aware of any non-compliance 48 hours after a SEF knows or reasonably

should know that it fails to satisfy its financial resources obligations rather than when the SEF submits its quarterly financial statement under § 37.1306(a), increasing the Commission's ability to promptly respond.

iii. Costs

Amended § 37.1301(a) reduces the amount of financial resources a SEF must maintain to an amount that will enable the SEF to comply with its core principle obligations and applicable Commission regulations for a one-year period, calculated on a rolling basis, rather than in an amount necessary to cover all of the SEF's operations as required under existing § 37.1301(a). The acceptable practices provide guidance on the costs that a SEF may exclude when determining its obligations under amended § 37.1301(a). As a result, amended § 37.1301(a) as supplemented by the acceptable practices likely will induce SEFs to reduce the current level of total financial resources that they maintain under § 37.1301. In turn, this could decrease market participants' confidence and could harm a SEF's stability during adverse market conditions because the SEF may not have adequate financial resources to cover its costs. However, the Commission believes the potential harm to a SEF's financial stability and to the market is minimal because amended § 37.1301(a) addresses only the amount of a SEF's total financial assets, which includes illiquid assets, rather than focusing only on a SEF's liquid assets. The Commission notes that illiquid assets are less important compared to the amount of liquid financial assets that a SEF must maintain under amended § 37.1303 since it is more difficult for a SEF to timely liquidate its illiquid assets to cover its operating costs, especially during periods of market instability. Accordingly, the Commission believes a SEF's liquid financial assets, which the Commission addresses in

amended § 37.1303 below, is more important for sustaining a SEF's financial health and continuing operations.

Amended § 37.1303 may require some SEFs to maintain additional liquid financial assets, compared to the current liquidity requirement, where a SEF's wind-down costs exceed six months of operating costs. However, as explained above in the discussion of benefits, the Commission believes most SEFs do not have wind-down costs that exceed six months of operating costs. Accordingly, amended § 37.1303 should not increase the liquidity requirement for most SEFs.

Amended § 37.1304 requires a SEF to incur an additional marginal cost to calculate its wind-down costs, in addition to its projected operating costs as currently required, in order to determine its financial resources obligations under §§ 37.1301 and 37.1303. The Commission estimates this change will impose an initial, minimal, one-time cost for each SEF related to determining the length of time and associated costs associated with an orderly wind down.

The Commission anticipates amended § 37.1306(a) will impose greater costs on a SEF. Specifically, amended § 37.1306(a) requires a SEF to submit U.S. GAAP-compliant quarterly reports. Because U.S. GAAP-compliant financial statements generally require additional effort compared to financial statements that are not U.S. GAAP -compliant, the Commission estimates the proposed change will increase annual costs for each SEF required to create U.S. GAAP-compliant financial reports.

The Commission does not believe amended § 37.1306(c) will increase costs. Under existing § 37.1306(c), a SEF must provide sufficient documentation explaining the methodology it used to compute its financial resources requirements; accordingly,

amended § 37.1306(c) is merely clarifying the type of information that is already required.[248] Similarly, the Commission does not believe amended § 37.1306(e) will materially increase costs since a SEF currently is required to maintain continuous compliance with its financial resources obligations. By requiring a SEF to notify the Commission within 48 hours of non-compliance, rather than informing the Commission through a SEF's quarterly financial submission, amended § 37.1306(e) could impose a *de minimis* cost to prepare a notice from a non-compliant SEF.

iv. Section 15(a) Factors

(1) Protection of Market Participants and the Public

The Commission previously noted that the financial resources requirements protect market participants and the public by establishing uniform standards and a system of Commission oversight that ensures trading occurs on a financially stable facility, which in turn, mitigates the risk of market disruptions, financial losses, and system problems that could arise from a SEF's failure to maintain adequate financial resources.[249] In the event that a SEF must wind down its operations, amended § 37.1303 explicitly requires a SEF to maintain sufficient liquid financial resources to conduct an orderly wind down of its operations, or three months of operating costs if greater than the SEF's wind-down costs.[250] The Commission believes the amended SEF financial requirements are better calibrated to the inherent risks of a SEF, and should result in greater efficiencies, but should not diminish the financial integrity of the SEF.

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[248] *See* § 37.1306(c).

[249] *See* Core Principles Final Rule at 33580.

[250] As the Commission previously noted, a SEF with sufficient amounts of liquid financial resources would be better positioned to close out trading in a manner not disruptive to market participants or to members of the public who rely on SEF prices. *See* Core Principles Final Rule at 33580.

Moreover, under amended § 37.1306(e), a SEF is required to provide notice no later than 48 hours after it knows or reasonably should know that it no longer satisfies its financial resources obligations, ensuring that the Commission can take prompt action to protect market participants and the public. In contrast, the Commission currently is notified of non-compliance in a SEF's quarterly financial statements. Lastly, a SEF is required to submit U.S. GAAP-compliant quarterly financial submissions under amended § 37.1306(c) that explicitly identify the costs a SEF has excluded or prorated in determining its projected operating costs. As a result, the Commission will more easily be able to compare SEFs' financial health and take proactive steps to protect market participants and the public if the Commission identifies a SEF with weak financial health or the development of negative financial trends among SEFs that could endanger market participants or the public.

(2) Efficiency, Competitiveness, and Financial Integrity of the Markets

Amended § 37.1301(a) and § 37.1303, as further supplemented through the acceptable practices, together should benefit market efficiency by reducing capital costs since SEFs are no longer required to maintain an excessive amount of financial resources. Accordingly, a SEF should be able to more efficiently allocate its financial resources, which in turn should encourage market growth and innovation. For example, as noted above, in the case of amended § 37.1303, the Commission expects most SEFs will need to hold approximately 50 percent less liquid financial assets as reserve capital to cover operating costs. The existing financial resources requirements can pose a burden to a SEF that wishes to innovate, because they will impose higher capital requirements if the SEF wishes to offer new or experimental technology, execution methods, or related products

and services. This is especially so if such business lines, products, or services are not expected to be immediately profitable or would have low margins.

The existing regulations may also discourage a SEF from offering more capital intensive activities, such as execution methods that involve human brokers compared to fully electronic trading that is less capital intensive. Accordingly, the Commission believes the amended financial resources requirements will be more neutral with respect to a SEF's chosen technology and business model, and therefore should encourage a greater variety of execution methods and related services and products in the market place.

Reducing capital costs may promote the entry of new entrants into the market by reducing start-up costs and initial capital requirements, thereby further encouraging competition and innovation. The increase in competition and innovation would depend on the extent to which potential new entrants respond to this encouragement.

Amended § 37.1306(e) should improve the financial integrity of markets by requiring a SEF to notify the Commission within 48 hours after it knows or reasonably should know that it no longer satisfies its financial resources obligations, ensuring that the Commission can take prompt action to protect market integrity. Lastly, amended § 37.1306(c) improves SEF financial submissions by requiring U.S. GAAP-compliant statements as well as clarifying that a SEF must explicitly identify any costs that it has excluded or prorated in determining its projected operating costs. These changes should improve the Commission's ability to conduct its oversight responsibilities to protect market integrity.

(3) Price Discovery

The Commission has not identified any effects of these rules on price discovery.

(4) Sound Risk Management Practices

By establishing specific standards with respect to how SEFs should assess and monitor the adequacy of their financial resources, the financial resources rules should promote sound risk management practices by SEFs. As noted above, amended § 37.1303 requires a SEF to identify its wind-down costs and associated timing and ensure it has sufficient liquid assets to maintain an orderly wind down. Similarly, amended § 37.1306(c) requires a SEF to explain the basis of its determination for its estimate of its wind-down costs and timing. Amended § 37.1306(e) requires a SEF to notify the Commission no later than 48 hours after it knows or reasonably should know it no longer satisfies its financial resources obligations. As a result, SEFs will be required to ensure they maintain the necessary procedures to identify, and to notify the Commission of, any non-compliance.

(5) Other Public Interest Considerations

The Commission has not identified any effects that these rules will have on public interest considerations other than those enumerated above, nor did any commenter suggest one.

v. Consideration of Alternatives and Comments

The Proposed Rule included requests for comment regarding possible alternatives to the proposed reporting requirements for SEFs. These included whether to require that a SEF's financial reports be audited, and whether financial reporting should be required on a semiannual rather than a quarterly basis.

WMBAA objected to the alternative of requiring that a SEF's financial reports be audited, contending, as discussed further above, that auditing reports would not improve oversight (*i.e.*, would not provide benefits).[251] WMBAA also argued the costs associated with an audited report are high and would pose a barrier to entry for new SEFs.[252] The Commission has determined not to adopt a requirement that SEF financial reports be audited.

Regarding the frequency of reports, WMBAA stated the current reporting requirement of quarterly financial reports is sufficient for ensuring capital adequacy, but that a semi-annual or annual report would also be adequate if a SEF is required to maintain all related documents and support for further inspection.[253] The Commission received no further comments comparing the costs and benefits of quarterly reporting to those of less frequent reporting. The Commission has determined to retain the existing quarterly reporting requirement for SEFs so that the Commission can remain abreast of a SEF's financial condition in a timely manner.

As noted above, commenters generally supported the proposed financial resources rules and offered no relevant alternatives other than those discussed above.[254] Accordingly, the Commission is generally finalizing the financial resources rules as proposed. However, there are two proposed provisions that the Commission has determined not to include in the Final Rules.

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[251] 2019 WMBAA Letter at 21.
[252] *Id*.
[253] *Id*.
[254] Commenters did suggest several possible rules that, as discussed above, are beyond the scope of this rulemaking. Should the Commission propose any of these alternatives in the future, it will consider their costs and benefits at that time.

First, the Proposed Rule included amendments to § 37.1301(b), which requires a SEF that also operates as a DCO to also comply with the financial resource requirements for DCOs under § 39.11. Specifically, the Commission proposed to amend § 37.1301(b) to permit SEFs that also operate as DCOs to file a single financial report under § 39.11 that covers both the SEF and DCO. The Commission is not finalizing this proposed change as part of the Final Rules but is continuing to consider it.

Second, the proposed acceptable practices included a provision that would have allowed a SEF offering more than one bona fide execution method to include the costs of only one of those methods in calculating projected operating costs, with the goal of mitigating the burden for SEFs wishing to offer multiple execution methods. This proposed change was intended to be consistent with the Proposed Rule's removal of existing limitations on execution methods for Required Transactions. The Final Rules are not implementing the Proposed Rule's expansion of permissible execution methods for Required Transactions, nor is it eliminating the minimum trading functionality requirement that a SEF maintain an Order Book as one of its execution methods. Accordingly, the Commission is not finalizing this particular proposed acceptable practice at this time.

5. Chief Compliance Officer

i. Overview

The Commission is adopting several amendments to the CCO regulations. First, the Commission is allowing the senior officer[255] of a SEF to have the same oversight

[255] As discussed below, the Commission proposes to define senior officer to mean the chief executive officer or other equivalent officer of the SEF.

responsibilities with respect to the CCO as the SEF's board of directors. Specifically, the Commission is (i) amending existing § 37.1501(b)(1)(i) to allow a CCO to consult with either the board of directors or senior officer of the SEF as the CCO develops the SEF's policies and procedures; (ii) amending existing § 37.1501(c)(1)(iii)[256] to allow a CCO to meet with either the senior officer of the SEF or the board of directors on an annual basis; (iii) amending existing § 37.1501(c)(1)(iv)[257] to allow a CCO to provide self-regulatory program information to the SEF's senior officer or to the board of directors; and (iv) eliminating the restriction under existing § 37.1501(c)(3) that removal of the CCO requires approval of a majority of the board of directors or the senior officer if the SEF does not have a board of directors, and instead permitting the board of directors or the senior officer to remove the CCO under § 37.1501(b)(3)(i).

Second, the Commission is consolidating and amending existing § 37.1501(d)(5) and (6)[258] to allow a CCO to identify noncompliance matters through "any means," in addition to the currently prescribed detection methods, and to clarify that the procedures followed to address noncompliance issues must be "reasonably designed" by the CCO to handle, respond, remediate, retest, and resolve noncompliance issues identified by the CCO. The Commission is also amending the CCO's duty to resolve conflicts of interest under existing § 37.1501(d)(2).[259] The Commission is refining the scope of the CCO's duty to take "reasonable steps" to resolve "material" conflicts of interest that may arise.

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[256] This requirement is in amended § 37.1501(b).

[257] This requirement is in amended § 37.1501(b)(6).

[258] This requirement is in amended § 37.1501(c)(5).

[259] This requirement is in amended § 37.1501(c)(2).

Third, the Commission is making certain amendments to the ACR regulations in existing § 37.1501(e)[260] in order to remove duplicative or unnecessary information requirements and streamline existing requirements. The Commission is removing existing § 37.1501(e)(2)(i), which requires a SEF to include in the ACR a review of all of the Commission regulations applicable to the SEF and identify the written policies and procedures designed to ensure compliance with the Act and Commission regulations. The Commission is also eliminating certain specific content required under existing § 37.1501(e)(4).[261] The Commission is amending existing § 37.1501(e)(5)[262] to require a SEF to only discuss material noncompliance matters and explain the corresponding actions taken to resolve such matters, rather than describing all compliance matters. The Commission is amending existing § 37.1501(e)(6)[263] to limit a SEF CCO's certification of an ACR's accuracy and completeness to "all material respects" of the report, rather than the entire report. The Commission is streamlining and reorganizing the remaining ACR content requirements, including consolidating the CCO's required description of the SEF's policies and procedures under existing § 37.1501(e)(1)[264] with the CCO's required assessment of the effectiveness of these policies and procedures under existing § 37.1501(e)(2)(ii), and consolidating the CCO's required narrative of any material changes made during the prior year along with any recommended potential or prospective changes

[260] This requirement is in amended § 37.1501(d).

[261] This requirement is in amended § 37.1501(d)(3). The eliminated provisions currently require a discussion of the SEF's compliance staffing and structure, a catalogue of investigations and disciplinary actions taken over the last year, and a review of disciplinary committee and panel performance.

[262] This requirement is in amended § 37.1501(d)(4).

[263] This requirement is in amended § 37.1501(d)(5).

[264] This requirement is in amended § 37.1501(d)(1).

and areas of improvement to the compliance program as required under existing § 37.1501(e)(3) and existing § 37.1501(e)(2)(iii),[265] respectively.

The Commission is finalizing several amendments to simplify the ACR submission procedures. The Commission is amending existing § 37.1501(f)(2)[266] to provide SEFs with an additional 30 days to file the ACR with the Commission. Additionally, the Commission is eliminating the "substantial and undue hardship" standard required for ACR extension requests and replacing it with a "reasonable and valid" standard set forth in existing § 37.1501(f)(4).[267] The Commission is amending existing § 37.1501(f)(3)[268] to require that the CCO submit an amended ACR to the SEF's board of directors or, in the absence of a board of directors, the senior officer of the SEF, for review prior to submitting the amended ACR to the Commission.

In addition to these substantive changes, the Commission is adopting a number of conforming, clarifying, and streamlining changes that would not impose new costs or result in new benefits and are not discussed below. The Commission is eliminating the CCO's obligations to the ROC, including existing § 37.1501(c)(1)(iii), which requires a quarterly meeting with the ROC and existing § 37.1501(c)(1)(iv), which requires the CCO to provide self-regulatory program information to the ROC. The Final Rule will not impact SEFs as there is no requirement that a SEF have a ROC.

Additionally, the Commission is consolidating existing § 37.1501(b) and (c) into final § 37.1501(b). The Commission is eliminating existing § 37.1501(b)(1), which

[265] This requirement is in amended § 37.1501(d)(2).

[266] This requirement is in amended § 37.1501(e)(2).

[267] This requirement is in amended § 37.1501(e)(4).

[268] This requirement is in amended § 37.1501(e)(3).

requires a SEF to designate a CCO and existing § 37.1501(c)(2), which requires the CCO to report directly to the board of directors or the senior officer of the SEF, as these requirements are already contained under § 37.1500.

The Commission is eliminating the requirement under existing § 37.1501(f)(1) that a SEF document the submission of the ACR to the SEF's board of directors or senior officer in the board minutes or some other similar written record. This requirement is already covered in the general recordkeeping requirements in amended § 37.1501(f), which is existing § 37.1501(g).

The Commission is finalizing an amendment to § 37.1501(a)(2) to define a "senior officer" as "the chief executive officer or other equivalent officer of the swap execution facility."[269] Finally, the Commission is adopting a new acceptable practice to Core Principle 15 in Appendix B that provides a non-exclusive list of factors that a SEF may consider when evaluating an individual's qualifications to be a CCO.[270] This acceptable practice will provide a safe harbor and not impose new obligations.

ii. Benefits

The amendments give the senior officer the same authority as the board of directors to oversee the CCO and provide SEFs with greater opportunity to structure the management and oversight of the CCO based on the SEF's particular corporate structure, size, and complexity. This could increase efficiency and reduce costs. Additionally, the

[269] In the SEF Core Principles Final Rule, the Commission did not adopt a definition of "senior officer," but noted that the statutory term would only include the most senior executive officer of the legal entity registered as a SEF. *See* SEF Core Principles Final Rule at 33544.

[270] 17 CFR part 37 app. B.

quality of oversight of the CCO could improve if the senior officer is better positioned than the board of directors to provide day-to-day oversight of the CCO.

The amendments permit a CCO to use any means to identify noncompliance issues and are less prescriptive than the existing rule, which could increase efficiency and reduce costs. The amendment to § 37.1501(d) refines the scope of the required information in an ACR and should make the ACR process more efficient and reduce costs. The removal of § 37.1501(e)(2)(i) and certain specific content set forth under § 37.1501(e)(4) should reduce the amount of time that a CCO and his or her staff spend preparing the ACR.

Amended § 37.1501(d)(4), which requires SEFs to focus on describing material non-compliance matters, rather than describing all compliance matters, should streamline the ACR requirement and provide more useful information to the Commission. Additionally, the clarification under § 37.1501(e)(3) that the CCO must submit an amended ACR to the SEF's board of directors or, in the absence of a board of directors, the senior officer of the SEF, should reduce the need for extensive follow-up discussions.

Finally, the amendment allowing SEFs more time to submit their ACRs should reduce the time and resource burden on CCOs and SEFs' compliance departments. This additional time should allow SEFs to fully complete their ACRs and meet their other end-of-year reporting obligations such as the fourth-quarter financial report. However, the Commission understands that those SEFs that already may rely on Commission staff no-action relief for an extra 30 days to complete the ACR may have already availed themselves of the benefits associated with the extended reporting deadline.

iii. Costs

The amendments to § 37.1501(b) that authorize the senior officer to oversee the CCO could impair the independence of the CCO, and as a result, the CCO's oversight of the SEF. However, the Commission believes this concern is mitigated by the Commission's review of annual ACRs and its examination program.

The amendments eliminate requirements that the CCO identify noncompliance matters using certain specified detection methods, design procedures that detect and resolve all possible noncompliance issues, and eliminate all potential conflicts of interest. These requirements are replaced by more flexible standards, which could potentially allow for some impairment of a CCO's oversight of the SEF's compliance in some circumstances. However, the Commission believes the resulting costs (in the form of potential adverse consequences) will not be material because the amendments require a CCO to focus on material aspects of the compliance program (*e.g.*, material breaches and material conflicts of interest). The Commission believes placing the focus on material compliance issues, rather than all compliance issues, will not adversely impact SEF compliance.

The amendments to § 37.1501(e) that reduce the information required in an ACR could make it more difficult for the Commission to assess a SEF's compliance and self-regulatory programs. However, the Commission does not anticipate that these changes will materially impact the Commission's assessment, as the Commission already receives or has access to such information from other sources. For example, the Commission approves the SEF's compliance staffing and structure as part of the SEF's registration or rule submission, and annual updates provide minimal additional information, at best. In

addition, SEFs report finalized disciplinary actions to the NFA,[271] and the Commission is able to access this information through its oversight of the NFA.

Finally, the amendment providing SEFs more time to submit their ACRs could delay the Commission recognizing and addressing a SEF compliance issue. However, the Commission anticipates that such risk is mitigated to the extent that SEFs submit ACRs on the timeline set forth in the Final Rules. The Commission's experience has not indicated that delayed reporting pursuant to Commission staff no-action relief has adversely impacted its ability to recognize and address compliance issues in a timely manner.

iv. Section 15(a) Factors

(1) Protection of Market Participants and the Public

The Commission believes the changes to the existing SEF CCO requirements are likely to better enable the Commission to protect market participants and the public. Specifically, the Commission should be better able to assess whether a SEF's policies and procedures adversely impact a SEF's operations or its ability to comply with the core principles or Commission's regulations, which are intended in part to protect market participants.

The changes to the ACR requirements under amended § 37.1501(d) should better enable the Commission to assess the effectiveness of a SEF's compliance and self-regulatory programs; this assessment is intended, in part, to protect market participants. The amendments will remove some of the duplicative and unnecessary content

[271] *See* § 9.11 (which states that whenever an exchange decision pursuant to which a disciplinary action or access denial action is to be imposed has become final, the exchange must, within 30 days thereafter, provide written notice of such action to the person against whom the action was taken and notice to the National Futures Association). 17 CFR 9.11.

requirements and require the ACR to focus on describing material non-compliance matters. The Commission believes the new requirements will streamline the ACR and provide more useful information to the Commission. Removing these information requirements, *e.g.*, requirements to review all Commission regulations applicable to a SEF and to identify the written policies and procedures enacted to foster compliance, will likely reduce the amount of information in an ACR. However, the Commission has determined, based on its experience with the existing requirements, that this information generally does not enhance the usefulness of the ACR.

(2) Efficiency, Competitiveness, and Financial Integrity of Markets

The Commission is promoting the efficiency and integrity of a SEF's market by allowing a more streamlined compliance approach that does not require the board of directors to assume primary oversight responsibility for the CCO. This streamlined approach should, in many circumstances, permit CCOs to more efficiently make changes to the regulatory program in response to potential trading violations, which should aid in protecting the financial integrity of the market. Furthermore, the focus of CCOs' duties on reasonably designed procedures to address noncompliance issues and material conflicts of interest should improve CCOs' effectiveness by specifying that this is the appropriate standard. This increased effectiveness should permit CCOs to better allocate resources to focus on detecting and deterring material rule violations, which otherwise may harm the market's efficiency, competitiveness, and integrity.

(3) Price Discovery

The Commission believes the changes to the CCO requirements will not impede a CCO's ability to ensure compliance and are unlikely to have a substantial impact on price discovery.

(4) Sound Risk Management Practices

The Commission believes the new CCO rules should promote sound risk management practices. The gains in this regard will depend on the quality and effective implementation of the policies and practices that SEFs currently have in place and the new policies and procedures that they will adopt due to the proposed amendments.

(5) Other Public Interest Considerations

The Commission has not identified any effects that these rules will have on public interest considerations other than those enumerated above, nor did any commenter suggest one.

v. Consideration of Alternatives and Comments

Commenters support the proposed changes. WMBAA supports the amendments to add a definition of senior officer,[272] to amend the CCO's duties,[273] to the preparation of the ACR,[274] and to the ACR submission requirements.[275] Refinitiv supports the amendments to the preparation of the ACR.[276] The Commission did not receive any comments on the proposed amendments to the CCO's recordkeeping requirements.

[272] 2019 WMBAA Letter at 23.

[273] *Id.* at 25.

[274] *Id.* at 26.

[275] *Id.* at 27.

[276] Refinitiv Letter at 14.

The Commission also proposed to eliminate the existing enumerated conflicts of interest to avoid any inference that they are an exhaustive list of conflicts that a CCO must address. The Commission has determined that the list of potential conflicts that a CCO should resolve under existing § 37.1500(d)(2) does not create confusion, but instead provides useful examples, and the list will not be eliminated as proposed.

D. Antitrust Considerations

Section 15(b) of the CEA requires the Commission to take into consideration the public interest to be protected by the antitrust laws and endeavor to take the least anticompetitive means of achieving the purposes of the CEA, in issuing any order or adopting any Commission rule or regulation.[277] In the notice of proposed rulemaking, the Commission requested comments on whether: (1) the proposed rulemaking implicates any other specific public interest to be protected by the antitrust laws; (2) the proposed rulemaking is anticompetitive; and (3) there are less anticompetitive means of achieving the relevant purposes of the CEA.

The Commission does not anticipate that the amendments to part 37 that it is adopting in this rule will result in anticompetitive behavior. The Commission received no comments on the antitrust considerations of the proposed rules finalized herein.

List of Subjects in 17 CFR Part 37

Swap execution facilities.

For the reasons stated in the preamble, the Commodity Futures Trading Commission amends 17 CFR part 37 as follows:

[277] 7 U.S.C. 19(b).

PART 37 – SWAP EXECUTION FACILITIES

1. The authority citation for Part 37 continues to read as follows:

Authority: 7 U.S.C. 1a, 2, 5, 6, 6c, 7, 7a-2, 7b-3, and 12a, as amended by Titles VII and VIII of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111-203, 124 Stat. 1376.

2. Amend § 37.205 by revising paragraph (a) and removing paragraph (b)(2)(iv), the revision to read as follows:

§ 37.205 Audit trail.

(a) *Audit trail required.* A swap execution facility shall capture and retain all audit trail data necessary to detect, investigate, and prevent customer and market abuses. Such data shall be sufficient to reconstruct all indications of interest, requests for quotes, orders, and trades within a reasonable period of time and to provide evidence of any violations of the rules of the swap execution facility. An acceptable audit trail shall also permit the swap execution facility to track a customer order from the time of receipt through execution on the swap execution facility.

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3. Revise subpart N to read as follows:

Subpart N—Financial Resources

Sec.
37.1300 Core Principle 13—Financial resources.
37.1301 General requirements.
37.1302 Types of financial resources.
37.1303 Liquidity of financial resources.
37.1304 Computation of costs to meet financial resources requirement.
37.1305 Valuation of financial resources.
37.1306 Reporting to the Commission.
37.1307 Delegation of authority.

§ 37.1300 Core Principle 13—Financial resources.

(a) *In general.* The swap execution facility shall have adequate financial, operational, and managerial resources to discharge each responsibility of the swap execution facility.

(b) *Determination of resource adequacy.* The financial resources of a swap execution facility shall be considered to be adequate if the value of the financial resources exceeds the total amount that would enable the swap execution facility to cover the operating costs of the swap execution facility for a one-year period, as calculated on a rolling basis.

§ 37.1301 General requirements.

(a) A swap execution facility shall maintain financial resources on an ongoing basis that are adequate to enable it to comply with the core principles set forth in section 5h of the Act and any applicable Commission regulations. Financial resources shall be considered adequate if their value exceeds the total amount that would enable the swap execution facility to cover its projected operating costs necessary for the swap execution facility to comply with section 5h of the Act and applicable Commission regulations for a one-year period, as calculated on a rolling basis pursuant to § 37.1304.

(b) An entity that operates as both a swap execution facility and a derivatives clearing organization shall also comply with the financial resource requirements of § 39.11 of this chapter.

§ 37.1302 Types of financial resources.

Financial resources available to satisfy the requirements of § 37.1301 may include:

(a) The swap execution facility's own capital, meaning its assets minus its liabilities calculated in accordance with generally accepted accounting principles in the United States; and

(b) Any other financial resource deemed acceptable by the Commission.

§ 37.1303 Liquidity of financial resources.

The financial resources allocated by the swap execution facility to meet the ongoing requirements of § 37.1301 shall include unencumbered, liquid financial assets (*i.e.,* cash and/or highly liquid securities) equal to at least the greater of three months of projected operating costs, as calculated on a rolling basis, or the projected costs needed to wind down the swap execution facility's operations, in each case as determined under § 37.1304. If a swap execution facility lacks sufficient unencumbered, liquid financial assets to satisfy its obligations under this section, the swap execution facility may satisfy this requirement by obtaining a committed line of credit or similar facility in an amount at least equal to such deficiency.

§ 37.1304 Computation of costs to meet financial resources requirement.

A swap execution facility shall each fiscal quarter, make a reasonable calculation of its projected operating costs and wind-down costs in order to determine its applicable obligations under §§ 37.1301 and 37.1303. The swap execution facility shall have reasonable discretion in determining the methodologies used to compute such amounts. The Commission may review the methodologies and require changes as appropriate.

§ 37.1305 Valuation of financial resources.

No less than each fiscal quarter, a swap execution facility shall compute the current market value of each financial resource used to meet its obligations under §§

37.1301 and 37.1303. Reductions in value to reflect market and credit risk ("haircuts") shall be applied as appropriate.

§ 37.1306 Reporting to the Commission.

(a) Each fiscal quarter, or at any time upon Commission request, a swap execution facility shall provide a report to the Commission that includes:

(1) The amount of financial resources necessary to meet the requirements of §§ 37.1301 and 37.1303, computed in accordance with the requirements of § 37.1304, and the market value of each available financial resource, computed in accordance with the requirements of § 37.1305; and

(2) Financial statements, including the balance sheet, income statement, and statement of cash flows of the swap execution facility.

(i) The financial statements shall be prepared in accordance with generally accepted accounting principles in the United States, prepared in English, and denominated in U.S. dollars.

(ii) The financial statements of a swap execution facility that is not domiciled in the United States, and is not otherwise required to prepare financial statements in accordance with generally accepted accounting principles in the United States, may satisfy the requirement in paragraph (a)(2)(i) of this section if such financial statements are prepared in accordance with either International Financial Reporting Standards issued by the International Accounting Standards Board, or a comparable international standard as the Commission may otherwise accept in its discretion.

(b) The calculations required by paragraph (a) of this section shall be made as of the last business day of the swap execution facility's applicable fiscal quarter.

(c) With each report required under paragraph (a) of this section, the swap execution facility shall also provide the Commission with sufficient documentation explaining the methodology used to compute its financial requirements under §§ 37.1301 and 37.1303. Such documentation shall:

(1) Allow the Commission to reliably determine, without additional requests for information, that the swap execution facility has made reasonable calculations pursuant to § 37.1304; and

(2) Include, at a minimum:

(i) A total list of all expenses, without any exclusion;

(ii) All expenses and the corresponding amounts, if any, that the swap execution facility excluded or prorated when determining its operating costs, calculated on a rolling basis, required under §§ 37.1301 and 37.1303, and the basis for any determination to exclude or prorate any such expenses;

(iii) Documentation demonstrating the existence of any committed line of credit or similar facility relied upon for the purpose of meeting the requirements of § 37.1303 (*e.g.*, copies of agreements establishing or amending a credit facility or similar facility); and

(iv) All costs that a swap execution facility would incur to wind down the swap execution facility's operations, the projected amount of time for any such wind-down period, and the basis of its determination for the estimation of its costs and timing.

(d) The reports and supporting documentation required by this section shall be filed not later than 40 calendar days after the end of the swap execution facility's first three fiscal quarters, and not later than 90 calendar days after the end of the swap

execution facility's fourth fiscal quarter, or at such later time as the Commission may permit, in its discretion, upon request by the swap execution facility.

(e) A swap execution facility shall provide notice to the Commission no later than 48 hours after it knows or reasonably should know that it no longer meets its obligations under § 37.1301 or § 37.1303.

§ 37.1307 Delegation of authority.

(a) The Commission hereby delegates, until it orders otherwise, to the Director of the Division of Market Oversight or such other employee or employees as the Director may designate from time to time, authority to:

(1) Determine whether a particular financial resource under § 37.1302 may be used to satisfy the requirements of § 37.1301;

(2) Review and make changes to the methodology used to compute projected operating costs and wind-down costs under § 37.1304 and the valuation of financial resources under § 37.1305;

(3) Request reports, in addition to those required in § 37.1306, or additional documentation or information under § 37.1306(a), (c), and (e); and

(4) Grant an extension of time to file fiscal quarter reports under § 37.1306(d).

(b) The Director may submit to the Commission for its consideration any matter that has been delegated in this section. Nothing in this section prohibits the Commission, at its election, from exercising the authority delegated in this section.

4. Revise § 37.1501 to read as follows:

§ **37.1501 Chief compliance officer.**

(a) *Definitions.* For purposes of this part, the term—

Board of directors means the board of directors of a swap execution facility, or for those swap execution facilities whose organizational structure does not include a board of directors, a body performing a function similar to a board of directors.

Senior officer means the chief executive officer or other equivalent officer of the swap execution facility.

(b) *Chief compliance officer*—(1) *Authority of chief compliance officer.* (i) The position of chief compliance officer shall carry with it the authority and resources to develop, in consultation with the board of directors or senior officer, the policies and procedures of the swap execution facility and enforce such policies and procedures to fulfill the duties set forth for chief compliance officers in the Act and Commission regulations.

(ii) The chief compliance officer shall have supervisory authority over all staff acting at the direction of the chief compliance officer.

(2) *Qualifications of chief compliance officer.* (i) The individual designated to serve as chief compliance officer shall have the background and skills appropriate for fulfilling the responsibilities of the position.

(ii) No individual disqualified from registration pursuant to sections 8a(2) or 8a(3) of the Act may serve as a chief compliance officer.

(3) *Appointment and removal of chief compliance officer.* (i) Only the board of directors or the senior officer may appoint or remove the chief compliance officer.

(ii) The swap execution facility shall notify the Commission within two business days of the appointment or removal, whether interim or permanent, of a chief compliance officer.

(4) *Compensation of the chief compliance officer.* The board of directors or the senior officer shall approve the compensation of the chief compliance officer.

(5) *Annual meeting with the chief compliance officer.* The chief compliance officer shall meet with the board of directors or senior officer of the swap execution facility at least annually.

(6) *Information requested of the chief compliance officer.* The chief compliance officer shall provide any information regarding the self-regulatory program of the swap execution facility as requested by the board of directors or the senior officer.

(c) *Duties of chief compliance officer.* The duties of the chief compliance officer shall include, but are not limited to, the following:

(1) Overseeing and reviewing compliance of the swap execution facility with section 5h of the Act and any related rules adopted by the Commission;

(2) Taking reasonable steps, in consultation with the board of directors or the senior officer of the swap execution facility, to resolve any material conflicts of interest that may arise, including, but not limited to:

(i) Conflicts between business considerations and compliance requirements;

(ii) Conflicts between business considerations and the requirement that the swap execution facility provide fair, open, and impartial access as set forth in § 37.202; and;

(iii) Conflicts between a swap execution facility's management and members of the board of directors;

(3) Establishing and administering written policies and procedures reasonably designed to prevent violations of the Act and the rules of the Commission;

(4) Taking reasonable steps to ensure compliance with the Act and the rules of the Commission;

(5) Establishing procedures reasonably designed to handle, respond, remediate, retest, and resolve noncompliance issues identified by the chief compliance officer through any means, including any compliance office review, look-back, internal or external audit finding, self-reported error, or validated complaint;

(6) Establishing and administering a compliance manual designed to promote compliance with the applicable laws, rules, and regulations and a written code of ethics for the swap execution facility designed to prevent ethical violations and to promote honesty and ethical conduct by personnel of the swap execution facility;

(7) Supervising the self-regulatory program of the swap execution facility with respect to trade practice surveillance; market surveillance; real time market monitoring; compliance with audit trail requirements; enforcement and disciplinary proceedings; audits, examinations, and other regulatory responsibilities (including taking reasonable steps to ensure compliance with, if applicable, financial integrity, financial reporting, sales practice, recordkeeping, and other requirements); and

(8) Supervising the effectiveness and sufficiency of any regulatory services provided to the swap execution facility by a regulatory service provider in accordance with § 37.204.

(d) *Preparation of annual compliance report.* The chief compliance officer shall, not less than annually, prepare and sign an annual compliance report that covers the prior fiscal year. The report shall, at a minimum, contain:

(1) A description and self-assessment of the effectiveness of the written policies and procedures of the swap execution facility, including the code of ethics and conflict of interest policies, to reasonably ensure compliance with the Act and applicable Commission regulations;

(2) Any material changes made to compliance policies and procedures during the coverage period for the report and any areas of improvement or recommended changes to the compliance program;

(3) A description of the financial, managerial, and operational resources set aside for compliance with the Act and applicable Commission regulations;

(4) Any material non-compliance matters identified and an explanation of the corresponding action taken to resolve such non-compliance matters; and

(5) A certification by the chief compliance officer that, to the best of his or her knowledge and reasonable belief, and under penalty of law, the annual compliance report is accurate and complete in all material respects.

(e) *Submission of annual compliance report and related matters*—(1) *Furnishing the annual compliance report prior to submission to the Commission.* Prior to submission to the Commission, the chief compliance officer shall provide the annual compliance report for review to the board of directors of the swap execution facility or, in the absence of a board of directors, to the senior officer of the swap execution facility. Members of the board of directors and the senior officer shall not require the chief compliance officer to make any changes to the report.

(2) *Submission of annual compliance report to the Commission.* The annual compliance report shall be submitted electronically to the Commission not later than 90

calendar days after the end of the swap execution facility's fiscal year. The swap execution facility shall concurrently file the annual compliance report with the fourth-quarter financial report pursuant to § 37.1306.

(3) *Amendments to annual compliance report.* (i) Promptly upon discovery of any material error or omission made in a previously filed annual compliance report, the chief compliance officer shall file an amendment with the Commission to correct the material error or omission. The chief compliance officer shall submit the amended annual compliance report to the board of directors, or in the absence of a board of directors, to the senior officer of the swap execution facility, pursuant to paragraph (e)(1) of this section.

(ii) An amendment shall contain the certification required under paragraph (d)(5) of this section.

(4) *Request for extension.* A swap execution facility may request an extension of time to file its annual compliance report from the Commission. Reasonable and valid requests for extensions of the filing deadline may be granted at the discretion of the Commission.

(f) *Recordkeeping.* The swap execution facility shall maintain all records demonstrating compliance with the duties of the chief compliance officer and the preparation and submission of annual compliance reports consistent with §§ 37.1000 and 37.1001.

(g) *Delegation of authority.* The Commission hereby delegates, until it orders otherwise, to the Director of the Division of Market Oversight or such other employee or employees as the Director may designate from time to time, the authority to grant or deny

a request for an extension of time for a swap execution facility to file its annual compliance report under paragraph (e)(4) of this section. The Director may submit to the Commission for its consideration any matter that has been delegated in this paragraph. Nothing in this paragraph prohibits the Commission, at its election, from exercising the authority delegated in this paragraph.

5. In Appendix B to Part 37, under the heading "Core Principle 13 of Section 5h of the Act—Financial Resources," add paragraph (b), and under the heading "Core Principle 15 of Section 5h of the Act—Designation of Chief Compliance Officer," add paragraph (b), to read as follows:

Appendix B to Part 37—Guidance on, and Acceptable Practices in, Compliance with Core Principles

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Core Principle 13 of Section 5h of the Act—Financial Resources

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(b) *Acceptable Practices*—(1) *Reasonable calculation of projected operating costs.* In connection with a swap execution facility calculating its projected operating costs, the Commission has determined that a reasonable calculation should include all expenses necessary for the swap execution facility to comply with the core principles set forth in section 5h of the Act and any applicable Commission regulations. This calculation should be based on the swap execution facility's current level of business and business model, and should take into account any projected modification to its business model (*e.g.*, the addition or subtraction of business lines or operations or other changes), and any projected increase or decrease in its level of business over the next 12 months.

The Commission believes, however, that it may be reasonable for a swap execution facility to exclude the following expenses ("excludable expenses") from its projected operating cost calculations:

(i) Costs attributable solely to sales, marketing, business development, product development, or recruitment and any related travel, entertainment, event, or conference costs;

(ii) Compensation and related taxes and benefits for swap execution facility personnel who are not necessary to ensure that the swap execution facility is able to comply with the core principles set forth in section 5h of the Act and any applicable Commission regulations;

(iii) Costs for acquiring and defending patents and trademarks for swap execution facility products and related intellectual property;

(iv) Magazine, newspaper, and online periodical subscription fees;

(v) Tax preparation and audit fees;

(vi) To the extent not covered by paragraphs (b)(1)(ii) or (iii) of this Core Principle 13 of Section 5h of the Act—Financial Resources, the variable commissions that a voice-based swap execution facility may pay to its SEF trading specialists (as defined under § 37.201(c)), calculated as a percentage of transaction revenue generated by the voice-based swap execution facility. Unlike fixed salaries or compensation, such variable commissions are not payable unless and until revenue is collected by the swap execution facility; and

(vii) Any non-cash costs, including depreciation and amortization.

(2) *Prorated expenses.* The Commission recognizes that, in the normal course of a swap execution facility's business, there may be an expense (*e.g.*, typically related to overhead) that is only partially attributable to a swap execution facility's ability to comply with the core principles set forth in section 5h of the Act and any applicable Commission regulations; accordingly, such expense may need to be only partially attributed to the swap execution facility's projected operating costs. For example, if a swap execution facility's office rental space includes marketing personnel and compliance personnel, the swap execution facility may exclude the prorated office rental expense attributable to the marketing personnel. In order to prorate an expense, a swap execution facility should:

(i) Maintain sufficient documentation that reasonably shows the extent to which an expense is partially attributable to an excludable expense;

(ii) Identify any prorated expense in the financial reports that it submits to the Commission pursuant to § 37.1306; and

(iii) Sufficiently explain why it prorated any expense. Common allocation methodologies that can be used include actual use, headcount, or square footage. A swap execution facility may provide documentation, such as copies of service agreements, other legal documents, firm policies, audit statements, or allocation methodologies to support its determination to prorate an expense.

(3) *Expenses allocated among affiliates.* The Commission recognizes that a swap execution facility may share certain expenses with affiliated entities, such as parent entities or other subsidiaries of the parent. For example, a swap execution facility may share employees (including employees on secondment from an affiliate) that perform

similar tasks for the affiliated entities or may share office space with its affiliated entities. Accordingly, the Commission believes that it would be reasonable, for purposes of calculating its projected operating costs, for a swap execution facility to prorate any shared expense that the swap execution facility pays for, but only to the extent that such shared expense is actually attributable to the affiliate and for which the swap execution facility is reimbursed. Similarly, a reasonable calculation of a swap execution facility's projected operating costs must include the prorated amount of any expense paid for by an affiliated entity to the extent that the shared expense is attributable to the swap execution facility. In order to prorate a shared expense, the swap execution facility should:

(i) Maintain sufficient documentation that reasonably shows the extent to which the shared expense is attributable to and paid for by the swap execution facility and/or affiliated entity;

(ii) Identify any shared expense in the financial reports that it submits to the Commission; and

(iii) Sufficiently explain why it prorated any shared expense. A swap execution facility may provide documentation, such as copies of service agreements, other legal documents, firm policies, audit statements, or allocation methodologies, that reasonably shows how expenses are attributable to, and paid for by, the swap execution facility and/or its affiliated entities to support its determination to prorate an expense.

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Core Principle 15 of Section 5h of the Act—Designation of Chief Compliance Officer

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(b) *Acceptable Practices*—(1) *Qualifications of chief compliance officer*. In determining whether the background and skills of a potential chief compliance officer are appropriate for fulfilling the responsibilities of the role of the chief compliance officer, the swap execution facility has the discretion to base its determination on the totality of the qualifications of the potential chief compliance officer, including, but not limited to, compliance experience, related career experience, training, and any other relevant factors to the position. A swap execution facility should be especially vigilant regarding potential conflicts of interest when appointing a chief compliance officer.

(2) [Reserved]

Issued in Washington, DC, on December 23, 2020, by the Commission.

Christopher Kirkpatrick,

Secretary of the Commission.

NOTE: The following appendices will not appear in the Code of Federal Regulations.

Appendices to Swap Execution Facilities – Commission Voting Summary and Commissioners' Statements

Appendix 1 – Commission Voting Summary

On this matter, Chairman Tarbert and Commissioners Quintenz, Behnam, Stump, and Berkovitz voted in the affirmative. No Commissioner voted in the negative.

Appendix 2 – Statement of Concurrence of Commissioner Rostin Behnam

More than two years ago, in November 2018, the Commission voted to propose a comprehensive overhaul of the existing framework for swap execution facilities (SEFs).[1] Today, the Commission issues two rules finalizing aspects of the SEF Proposal and a withdrawal of the SEF Proposal's unadopted provisions. This is the final step in a long road. Last month, the Commission finalized rules emanating from the SEF Proposal regarding codification of existing no-action letters regarding, among other things, package transactions.[2] Today's final rules and withdrawal complete the Commission's consideration of the SEF Proposal.

Back in November 2018, I expressed concern that finalization of the SEF Proposal would reduce transparency, increase limitations on access to SEFs, and add significant costs for market participants.[3] I also noted that, while the existing SEF framework could benefit from targeted changes, particularly the codification of existing no-action relief, the SEF framework has in many ways been a success. I pointed out that the Commission's work to promote swaps trading on SEFs has resulted in increased liquidity, while adding pre-trade price transparency and competition. Nonetheless, I voted to put the SEF Proposal out for public comment, anticipating that the notice and comment process would guide the Commission in identifying a narrower set of changes

[1] Swap Execution Facilities and Trade Execution Requirement, 83 FR 61946 (Nov. 30, 2018) (the "SEF Proposal").

[2] Swap Execution Facility Requirements (Nov. 18, 2020), *https://www.cftc.gov/PressRoom/PressReleases/8313-20*.

[3] Statement of Concurrence of Commissioner Rostin Behnam Regarding Swap Execution Facilities and Trade Execution Requirement, *https://www.cftc.gov/PressRoom/SpeechesTestimony/behnamstatement110518a*.

that would improve the current SEF framework and better align it with the statutory mandate and the underling policy objectives shaped after the 2008 financial crisis.[4] More than two years and many comment letters later, that is exactly what has happened. The Commission has been precise and targeted in its finalization of specific provisions from the SEF Proposal that provide needed clarity to market participants and promote consistency, competitiveness, and appropriate operational flexibility consistent with the core principles.

In addition to expressing substantive concerns about the overbreadth of the SEF Proposal, I also voiced concerns that we were rushing by having a comparatively short 75-day comment period.[5] In the end, the comment period was rightly extended, and the Commission has taken the time necessary to carefully evaluate the appropriateness of the SEF Proposal in consideration of its regulatory and oversight responsibilities and the comments received. I think that the consideration of the SEF Proposal is an example of how the process is supposed to work. When we move too quickly toward the finish line and without due consideration of the surrounding environment, we risk making a mistake that will impact our markets and market participants.

Finally, I would like to address the Commission's separate vote to withdraw the unadopted provisions of the SEF Proposal. In the past, I have expressed concern with such withdrawals by an agency that has historically prided itself on collegiality and working in a bipartisan fashion.[6] In the case of today's withdrawal, the Commission has

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[4] *Id.*

[5] *Id.*

[6] Rostin Behnam, Commissioner, CFTC, Dissenting Statement of Commissioner Rostin Behnam Regarding Electronic Trading Risk Principles (June 25, 2020), *https://www.cftc.gov/PressRoom/SpeechesTestimony/behnamstatement062520b*.

voted on all appropriate aspects of the SEF Proposal through three rules finalized during the past month. The Commission has voted unanimously on all of these rules, including today's decision to withdraw the remainder from further consideration. While normally a single proposal results in a single final rule, in this instance, multiple final rules have been finalized emanating from the SEF Proposal. This could lead to confusion regarding the Commission's intentions regarding the many unadopted provisions of the SEF Proposal. Under such circumstances, I think it is appropriate to provide market participants with clarity regarding the SEF Proposal. Accordingly, I will support today's withdrawal of the SEF Proposal. But rather than viewing it as a withdrawal of the SEF Proposal, I see it as an affirmation of the success of the existing SEF framework and the careful process to markedly improve the SEF framework in a measured and thoughtful way.

Appendix 3 – Statement of Commissioner Dan M. Berkovitz

I support the Commission's decision to withdraw its 2018 proposal to overhaul the regulation of swap execution facilities ("SEFs")[1] ("2018 SEF NPRM") and proceed instead with targeted adjustments to our SEF rules ("Final Rules"). The two Final Rules approved today will make minor changes to SEF requirements while retaining the progress we have made in moving standardized swaps onto electronic trading platforms, which has enhanced the stability, transparency, and competitiveness of our swaps markets.[2]

[1] Swap Execution Facilities and Trade Execution Requirement, 83 FR 61946 (Nov. 30, 2018).

[2] Dissenting Statement of Commissioner Dan M. Berkovitz Regarding Proposed Rulemaking on Swap Execution Facilities and Trade Execution Requirement (Nov, 5, 2018), available at *https://www.cftc.gov/PressRoom/SpeechesTestimony/berkovitzstatement110518a*.

When the Commission issued the 2018 SEF NPRM, I proposed that we enhance the existing swaps trading system instead of dismantling it. For example, I urged the Commission to clarify the floor trader exception to the swap dealer registration requirement and abolish the practice of post-trade name give-up for cleared swaps. I am pleased that the Commission already has acted favorably on both of those matters. Today's rulemaking represents a further positive step in this targeted approach.

Many commenters to the 2018 SEF NPRM supported this incremental approach, advocating discrete amendments rather than wholesale changes. Today, the Commission is adopting two Final Rules that codify tailored amendments that received general support from commenters. The first rule—Swap Execution Facilities—amends part 37 to address certain operational challenges that SEFs face in complying with current requirements, some of which are currently the subject of no-action relief or other Commission guidance. The second rule—Exemptions from Swap Trade Execution Requirement—exempts two categories of swaps from the trade execution requirement, both of which are linked to exceptions to or exemptions from the swap clearing requirement.

Swap Execution Facilities: Audit Trail Data, Financial Resources and Reporting, and Requirements for Chief Compliance Officers

Commission regulations require a SEF to capture and retain all audit trail data necessary to detect, investigate, and prevent customer and market abuses, which currently includes identification of each account to which fills are ultimately allocated.[3] Following the adoption of these regulations, SEFs represented that they are unable to capture post-execution allocation data because the allocations occur away from the SEF, prompting

[3] 17 CFR 37.205(a), b(2)(iv).

CFTC staff to issue no-action relief. Other parties, including DCOs and account managers, must capture and retain post-execution allocation information and produce it to the CFTC upon request, and SEFs are required to establish rules that allow them obtain this allocation information from market participants as necessary to fulfill their self-regulatory responsibilities. Given that staff is not aware of any regulatory gaps that have resulted from SEFs' reliance on the no-action letter, codifying this alternative compliance framework is appropriate.

This Swap Execution Facility final rule also will amend part 37 to tie a SEF's financial resource requirements more closely to the cost of its operations, whether in complying with core principles and Commission regulations or winding down its operations. Based on its experience implementing the SEF regulatory regime, the Commission believes that these amended resource requirements—some of which simply reflect current practice—will be sufficient to ensure that a SEF is financially stable while avoiding the imposition of unnecessary costs. Additional amendments to part 37, including requirements that a SEF must prepare its financial statements in accordance with U.S. GAAP standards, identify costs that it has excluded in determining its projected operated costs, and notify the Commission within 48 hours if it is unable to comply with its financial resource requirements, will further enhance the Commission's ability to exercise it oversight responsibilities.

Finally, this rule makes limited changes to the Chief Compliance Officer ("CCO") requirements. As a general matter, I agree that the Commission should clarify certain CCO duties and streamline CCO reporting requirements where information is duplicative or not useful to the Commission. Although the CCO requirements diverge somewhat

from those for futures commission merchants and swap dealers, the role of SEFs is different and therefore, standardization is not always necessary or appropriate. I expect that the staff will continue to monitor the effects of all of the changes adopted today and inform the Commission if it believes further changes to our rules are needed.

Exemptions from Swap Trade Execution Requirement

Commodity Exchange Act ("CEA") section 2(h)(8) specifies that a swap that is excepted from the clearing requirement pursuant to CEA section 2(h)(7) is not subject to the requirement to trade the swap on a SEF. Accordingly, swaps that fall into the statutory swap clearing exceptions (e.g., commercial end-users and small banks) are also excepted from the trading mandate. However, the Commission has also exempted from mandatory clearing swaps entered into by certain entities (e.g., cooperatives, central banks, and swaps between affiliates) using different exemptive authorities from section 2(h)(7).

The Exemptions from Swap Trade Execution Requirement final rule affirms the link between the clearing mandate and the trading mandate for swaps that are exempted from the clearing mandate under authorities other than CEA section 2(h)(7). The additional clearing exemptions are typically provided by the Commission to limited types of market participants, such as cooperatives or central banks that use swaps for commercial hedging or have financial structures or purposes that greatly reduce the need for mandatory clearing and SEF trading. In addition, limited data provided in the release indicates that, at least up to this point in time, these exempted swaps represent a small percentage of the notional amount of swaps traded.

This final rule also exempts inter-affiliate swaps from the trade execution requirement. These swaps are exempted from the clearing requirement primarily because the risks on both sides of the swap are, at least in some respects, held within the same corporate enterprise. As described in the final rule release, these swaps may not be traded at arms-length and serve primarily to move risk from one affiliate to another within the same enterprise. Neither market transparency nor price discovery would be enhanced by including these transactions within the trade execution mandate. For these reasons, I am approving the Exemptions from Swap Trade Execution Requirement final rule as a sensible exemption consistent with the relevant sections of the CEA.

Conclusion

These two Final Rules provide targeted changes to the SEF regulations based on experience from several years of implementing them. These limited changes, together with the withdrawal of the remainder of the 2018 SEF NPRM, effectively leave in place the basic framework of the SEF rules as originally adopted by the Commission. This framework has enhanced market transparency, improved competition, lowered transaction costs, and resulted in better swap prices for end users. While it may be appropriate to make other incremental changes going forward, it is important that we affirm the established regulatory program for SEFs to maintain these benefits and facilitate further expansion of this framework.

I thank the staff of the Division of Market Oversight for their work on these two rules and their helpful engagement with my office.