

COMMODITY FUTURES TRADING COMMISSION**17 CFR Parts 9, 36, 37, 38, 39, and 43****RIN 3038–AE25****Swap Execution Facilities and Trade Execution Requirement****AGENCY:** Commodity Futures Trading Commission.**ACTION:** Proposed rule; withdrawal.

SUMMARY: On November 30, 2018, the Commodity Futures Trading Commission (“CFTC” or the “Commission”) published a “Swap Execution Facilities and Trade Execution Requirement” notice of proposed rulemaking (“NPRM”) in the *Federal Register*. While the Commission has adopted certain proposals from the NPRM, in light of feedback the Commission received in response to the remaining proposals in the NPRM, the Commission has determined to not proceed with those unadopted proposals relating to the regulation of swap execution facilities (“SEFs”) and the trade execution requirement (“Determination”). In separate final rules, the Commission adopted the following portions of the NPRM: two exemptions, pursuant to Commodity Exchange Act (“CEA”) section 4(c), from the trade execution requirement in CEA section 2(h)(8); and (2) final rules related to audit trail requirements for post-trade allocations, SEF financial resource requirements, and SEF chief compliance officer requirements (collectively, the “Final Rules”). As such, this withdrawal does not impact or alter any of those sections of the NPRM that are being adopted in the Final Rules, as described further in footnote 1 below. In light of the Determination, the Commission has decided to withdraw the unadopted portions of the NPRM.

DATES: The Commission is withdrawing proposed rules published in the *Federal Register* on November 30, 2018 (83 FR 61946) as of [INSERT DATE OF PUBLICATION IN THE *FEDERAL REGISTER*].

ADDRESSES: Comments previously submitted in response to the NPRM remain on file at the Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street NW, Washington, DC 20581 and may also be accessed via the CFTC Comments Portal: <https://comments.cftc.gov>.

FOR FURTHER INFORMATION CONTACT: Roger Smith, Associate Chief Counsel, Division of Market Oversight, (202) 418–5344, rsmith@cftc.gov, Commodity Futures Trading Commission, 525 West Monroe Street, Suite 1100, Chicago, IL 60661; or David E. Aron, Acting Associate Director, Division of Data, (202) 418-6621, daron@cftc.gov, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, NW, Washington, DC 20581.

SUPPLEMENTARY INFORMATION: On November 30, 2018, the Commission published the NPRM, which proposed a comprehensive foundational shift in the regulatory framework for SEFs.¹ In particular, if adopted, the NPRM would have, among other things, (i) required that certain swaps broking entities, including interdealer brokers, and aggregators of single-dealer platforms register as SEFs pursuant to the registration requirement under CEA section 5h(a)(1);² (ii) broadened the scope of the trade execution requirement, but provided certain exemptions; (iii) allowed a SEF to offer flexible execution methods for swaps subject to the trade execution requirement; and (iv)

¹See the NPRM, 83 FR 61946 (Nov. 30, 2018), available at: <https://www.cftc.gov/sites/default/files/2018-11/2018-24642a.pdf>.

² 7 U.S.C. 7b-3(a)(1).

established disclosure-based trading and execution rules applicable to any SEF execution method. In conjunction with flexible execution methods, the Commission also proposed limits on the scope of trading-related communications (“pre-execution communications”) that SEF participants may conduct away from a SEF’s trading system or platform, as well as proficiency requirements for certain SEF employees who facilitate trading.

Additionally, the Commission proposed amendments to impartial access rules that would provide a SEF with greater flexibility to structure its access requirements, and to tailor its rule enforcement program and disciplinary procedures and sanctions, to its trading operations and market. The proposed rules also would have made non-substantive amendments and various conforming changes to other Commission regulations.

In response to the NPRM, the Commission received fifty-six comment letters from SEFs, market participants, industry trade associations, public interest organizations, and other interested parties. The NPRM comprehensively sought to amend the SEF regulatory framework. For example, one commenter characterized the NPRM as a “fundamental reconstruction of the ‘SEF ecosystem,’” and “[the NPRM would] change many of the ways in which market participants interact with, and trade on, SEFs. This reconstruction of the existing ecosystem would present tall operational challenges and impose substantial costs on all market participants....”³ Several commenters expressed concern over the magnitude of changes behind the NPRM. Therefore, to avoid potential and unintended adverse market impacts caused by comprehensive and far-reaching changes, several commenters preferred that the Commission adopt a more “targeted” approach.

³ Futures Industry Association (“FIA”) Letter at 7.

The Commission, at the time, proposed the NPRM based on particular views regarding the need for a comprehensive revamping of the regulatory framework for SEFs. In light of feedback the Commission received in response to the NPRM, and upon further consideration, the Commission believes that rather than comprehensively amending the fundamentals underpinning the SEF regime, the Commission should instead work to improve the SEF framework through targeted rulemakings that address distinct issues. The Commission agrees with commenters that this approach will help the Commission avoid unintended adverse market impacts caused by the comprehensive and far-reaching changes of the NPRM.

Therefore, the Commission has determined to withdraw the unadopted portions of the pending NPRM in order to allow the Commission to propose and adopt targeted rulemakings to address specific SEF issues or requirements.⁴

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.

⁴ Concurrently with this withdrawal, the Commission is adopting the Final Rules to implement various proposals from the NPRM. One of the Final Rules adopted two CEA section 4(c) exemptions from the trade execution requirement. Specifically, this final rulemaking adopted proposed § 36.1(c) and § 36.1(e), which were respectively re-numbered as § 36.1(b) and § 36.1(c) in the adopting release. *See* Exemption from Swap Execution Requirement, published in yesterday's issue of the *Federal Register*. The other adopted various proposals related to audit trail requirements for post-trade allocations, SEF financial resource requirements, and SEF chief compliance officer requirements. In particular, these final rules addressed the proposals for §§ 37.205(a) and (b)(2); 37.1301; 37.1302; 37.1303; 37.1304; 37.1305; 37.1306; 37.1307; and 37.1501. *See* Swap Execution Facilities, published in yesterday's issue of the *Federal Register*. This withdrawal does not impact or alter any of the Final Rules.

**Appendices to Swap Execution Facilities and Trade Execution Requirement –
Commission Voting Summary, Chairman’s Statement, 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 Support of Chairman Heath P. Tarbert

Nearly two thousand years ago, the Stoic philosopher and statesman Seneca the Younger observed that “*every new beginning comes from some other beginning’s end.*” This remains as true today as it was then, and as it was in the 1990s when the band Semisonic built a song around it.

I vote today in support of withdrawing the remaining unadopted portions of the November 2018 Swap Execution Facilities (“SEF”) and Trade Execution Requirement proposal (“SEF Proposal”). With the beginning of a new SEF landscape based on other rules we are announcing today, it is appropriate to bring that proposal—which was itself a beginning of sorts—to an end.

The SEF Proposal, which was championed by my predecessor Chairman Chris Giancarlo, was comprehensive in that it sought to codify staff no-action relief and otherwise resolve operational concerns of SEFs and market participants. It also set forth structural reforms to the SEF regime beyond these operational fixes. The SEF Proposal reflected a great deal of time, effort, and thought, and resulted in several rules ultimately adopted by the Commission. I am grateful indeed for Chairman Giancarlo’s thought leadership and the path that the SEF Proposal set our agency upon.

In particular, our Commission yesterday adopted from the SEF Proposal: (1) two exemptions, pursuant to Commodity Exchange Act (“CEA”) section 4(c), from the trade execution requirement in CEA section 2(h)(8); and (2) final rules related to audit trail requirements for post-trade allocations, SEF financial resource requirements, and SEF chief compliance officer requirements. With respect to the unadopted portions of the SEF Proposal, the feedback received from market participants and the public made clear that moving forward would require significantly more work and a re-proposal of the rules. Therefore, I believe it is appropriate to withdraw those unadopted elements. Doing so is also consistent with our Commission’s reasoning for withdrawing Regulation AT a few months ago—we can start a new beginning only once we have ended the prior beginning.

Appendix 3 – Statement of Support of Commissioner Brian D. Quintenz

I will vote in favor of withdrawing the unadopted provisions from the Commission’s 2018 proposal comprehensively to amend the regulations applicable to swap execution facilities (SEFs)¹, but only because the Commission has already adopted many of these proposals, including in the areas of SEF financial resources, audit trail data, and exceptions to the trade execution requirement, so that the SEF ruleset becomes more practical for market participants. I note that many of the finalized provisions are based on longstanding no-action relief that has taken over eight years and a Republican administration to rationalize the inadequate ruleset left by the Commission’s prior leadership.

¹ SEFs and Trade Execution Requirement, 83 FR 61946 (Nov. 30, 2018).

I regret significantly, however, that certain aspects of the 2018 proposal have not been acted upon or debated as a Commission since. In particular, the CEA as amended by Dodd Frank, legally allows SEFs greater flexibility – specifically through “any means of interstate commerce”² – in which methods of execution they may offer for swaps subject to the trade execution requirement, than the overly prescriptive and government-knows-best requirement that a SEF may only provide either a RFQ-to-3 or a Central Limit Order Book (CLOB) trading mechanism, as dictated by an existing CFTC rule.³ Indeed, such flexibility was recently requested by a wide range of market participants during the period of COVID-inspired market volatility and thin liquidity.⁴ If such trade execution flexibility is necessary to support liquidity in a stressed environment, why would it not benefit the markets more generally in normal environments? Additionally, such flexibility is absolutely consistent with the definition of a SEF set forth in the CEA, that establishes a SEF as a multiple-to-multiple trading system.”⁵

Appendix 4 – 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

² Definition of SEF, sec. 1a(50) of the CEA.

³ CFTC reg. 37.9(a).

⁴ Comment letter from ISDA, dated May 22, 2020, in response to the Commission’s February 2020 proposal on SEF and Real-Time Reporting requirements (85 FR 9407 (Feb. 19, 2020)).

⁵ Definition of SEF, sec. 1a(50) of the CEA.

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

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 that would improve the current SEF framework and better align it with the statutory mandate and the underlying 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

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>.

⁴ *Id.*

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 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

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>.

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 5 – 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

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

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>.

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 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-

³ 17 CFR 37.205(a), b(2)(iv).

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 its 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 exempted 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.