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Staff Advisory on Swap Execution Facility Registration Requirement

The Division of Market Oversight (“DMO”) of the Commodity Futures Trading Commission (“Commission”) is issuing this advisory (“Advisory”) to remind entities of the swap execution facility (“SEF”) registration requirements set forth in the Commodity Exchange Act (“CEA”) and Commission regulations and to highlight certain scenarios where entities may be required to register.

This Advisory focuses on the application of the SEF registration requirement to entities: (1) facilitating trading or execution of swaps through one-to-many or bilateral communications; (2) facilitating trading or execution of swaps that are not subject to the trade execution requirement in CEA section 2(h)(8);¹ (3) providing non-electronic means for the execution of swaps; or (4) falling within the SEF definition and operated by an entity currently registered with the Commission in some other capacity, such as a commodity trading advisor (“CTA”) or an introducing broker. The determination whether a facility meets the requirements to register as a SEF depends on all relevant facts and circumstances of its operations.

A. Regulatory Background

CEA section 5h(a)(1) establishes the SEF registration requirement, providing 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 designated contract market (“DCM”).² In 2013, the Commission adopted a final rule entitled “Core Principles and Other Requirements for Swap Execution Facilities” (“2013 Final Rule”).³ The 2013 Final Rule includes Commission Regulation

¹ 7 U.S.C. 2(h)(8).

² 7 U.S.C. 7b-3(a)(1).

³ Core Principles and Other Requirements for Swap Execution Facilities, 78 FR 33476 (June 4, 2013). Although the Commission in November 2018 issued a proposed rulemaking to amend the various requirements established in the 2013 Final Rule, the Commission subsequently in February 2021 withdrew the remaining, unadopted portions of the November 2018 proposal. *See* Swap Execution Facilities and Trade Execution Requirement, 83 FR 61946 (Nov. 30, 2018) and Swap Execution Facilities and Trade Execution Requirement, 86 FR 9304 (Feb. 12, 2021) (“SEF Rule Withdrawal”), respectively. The adopted portions of the November 2018 proposal were directed at exemptions to the

37.3(a)(1),⁴ which sets forth the requirements for registration as a SEF. In the 2013 Final Rule, the Commission stated the statutory SEF registration requirement applies only to facilities meeting the SEF definition in CEA section 1a(50).⁵ CEA section 1a(50)⁶ defines a SEF as:

a trading system or platform in which multiple participants have the ability to execute or trade swaps by accepting bids and offers made by multiple participants in the facility or system, through any means of interstate commerce, including any trading facility⁷, that—
(A) Facilitates the execution of swaps between persons; and (B) is not a designated contract market.

DMO staff notes that the portion of the SEF statutory definition that states “in which multiple participants have the ability to execute or trade swaps by accepting bids and offers made by multiple participants in the facility or system”⁸ is referred to herein as the “multiple-to-multiple prong.”

B. Application of the Registration Requirement

1. Facilities offering one-to-many or bilateral communications

The multiple-to-multiple prong can be satisfied, and thus registration may be required, (i) even where multiple participants cannot *simultaneously* request, make, or accept bids and offers from multiple participants; or (ii) where multiple participants can initiate a one-to-many communication.⁹ Specifically, a facility meets the multiple-to-multiple prong if multiple participants have the “ability to execute or trade swaps” with multiple participants.¹⁰ In the 2013 Final Rule, the Commission stated a one-to-many system or platform on which the sponsoring entity is the counterparty to all swap contracts executed through the system or platform, and thus the provision of liquidity is limited to a single liquidity provider (*i.e.*, the sponsoring entity) does not provide the ability for participants to conduct multiple-to-multiple execution or trading.¹¹ In contrast, a one-to-many system or platform like a request for quote (“RFQ”) system—where a single requestor initiates for each transaction a one-to-many communication by submitting an RFQ to multiple participants—will satisfy the multiple-to-multiple prong if more than one participant is able to submit an RFQ on the platform.

trade execution requirement and certain audit trail, post-trade allocation, financial resource and chief compliance officer requirements. For clarity and the avoidance of any doubt, DMO staff, consistent with the SEF Rule Withdrawal, states that those unadopted portions of the November 2018 proposal have been withdrawn by the Commission, and therefore, do not affect the application of the 2013 Final Rule.

⁴ 17 CFR § 37.3(a)(1).

⁵ *Id.* at 33481.

⁶ 7 U.S.C. 1a(50).

⁷ 7 U.S.C. 1a(51).

⁸ 7 U.S.C. 1a(50).

⁹ The multiple-to-multiple prong is one component of the SEF registration requirement and is not determinative.

¹⁰ 7 U.S.C. 1a(50) (emphasis added).

¹¹ 2013 Final Rule at 33482. *See also id.* at 33481 n. 87. (“The SEF [Notice of Proposed Rulemaking] stated that certain entities such as one-to-one voice services and single-dealer platforms do not provide the ability for participants to conduct multiple-to-multiple execution or trading because they limit the provision of liquidity to a single liquidity provider.”).

On several occasions, DMO staff reviewed facilities enabling market participants to communicate bids and offers to other market participants through a “chat” function. Although each bid or offer was communicated on a one-to-one basis, DMO staff determined some of these facilities satisfied the multiple-to-multiple prong because multiple market participants were able to initiate a one-to-one communication and the participant could choose to send the communication to one or more market participants. Thus, the platforms enabled multiple market participants to accept bids and offers from multiple market participants. The determining factor of the multiple-to-multiple prong depends not on whether communications are bilateral or multilateral, but instead on whether more than one participant has the ability to execute or trade swaps by accepting bids and offers from more than one participant.¹²

Thus, a facility may satisfy the multiple-to-multiple prong even if (i) the facility permits only bilateral, or “one-to-one,” communications, and (ii) multiple participants cannot simultaneously request, make or accept bids and offers from multiple participants. Similarly, a facility may satisfy the multiple-to-multiple prong if the facility permits only “one-to-many” communications from which multiple participants can initiate a one-to-many communication.

2. Entities listing only swaps that are not subject to the trade execution requirement

DMO staff reminds entities that registration may be required if they operate a facility that meets the SEF definition, even if the facility facilitates the trading and execution only of swaps not subject to the trade execution requirement.¹³

3. Facilities offering non-electronic methods of trading

The SEF definition is not limited to a specific method of execution on the facility. Thus, facilities that meet the SEF definition and offer only non-electronic methods of trading may need to register as a SEF. As noted in the 2013 Final Rule, the Commission interpreted the phrase “through any means of interstate commerce” in the SEF definition in CEA section 1a(50) to mean the utilization of “a variety of means of execution or communication, including, but not limited to, telephones, internet communications, and electronic transmissions.”¹⁴

¹² If the multiple-to-multiple prong turned on whether participants were able to communicate with multiple liquidity providers simultaneously, facilities could limit communications to bilateral means in order to avoid the registration requirement. For example, a facility allowing a participant to press a button once to send a communication to multiple participants, instead could require the participant to press the button multiple times, once for each participant contacted. DMO staff believes the reasons for requiring SEF registration is identical in both situations, and does not believe Congress intended the Commission to disregard substance for form.

¹³ 7 U.S.C. 1a(50) and 7b–3(a)(1); *see also* 2013 Final Rule at 33481 n.88.

¹⁴ *Id.* at 33501 n.328.

4. Entities registered with the Commission in some other capacity

An entity that is registered with the Commission in another capacity, such as a CTA or introducing broker (“IB”), may be subject to the SEF registration requirement if it operates a facility that falls within the SEF definition. CEA sections 1a(50) and 5h(a)(1) provide an exception to the SEF registration requirement to entities registered as DCMs; there is no exception for entities otherwise registered with the Commission.¹⁵ To this end, DMO staff advises existing CFTC registered entities, such as CTAs and IBs, to review carefully their activities and evaluate whether they may be subject to the SEF registration requirement.

C. Conclusion

Whether a particular facility is required to register depends on all of the relevant facts and circumstances of the facility’s operations. DMO staff encourages entities falling within the categories discussed above to review their activities and assess whether they meet the SEF definition, thereby requiring SEF registration. DMO staff also encourages any person operating a facility for the trading or processing of swaps to reach out to DMO staff if they have questions about their activities and their potential obligation to register the facility as a SEF.¹⁶

This Advisory is intended to remind the affected parties of their obligations under the CEA and Commission regulations. The Advisory may include interpretations of the CEA and Commission regulations relating to whether an entity may be required to register as a SEF based on certain facts and circumstances. It is not intended to create any enforceable rights, any new binding registration rules or regulations, or to amend existing rules or regulations. This Advisory represents only the views of DMO staff and does not necessarily represent the views of the Commission or of any other division or office of the Commission. If you have any questions concerning this Advisory, please contact Nancy Markowitz, Deputy Director, Division of Market Oversight, at (202) 418-5453 or nmarkowitz@cftc.gov, or Jonathan Lave, Associate Director, Division of Market Oversight, at (202) 418-5983 or jlave@cftc.gov.

Sincerely,

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¹⁵ 7 U.S.C. 1a(50) and 7b–3(a)(1). Thus, a DCM may list swaps and offer a platform for trading and executing swaps, but not have to register as a SEF. 17 CFR § 37.3.

¹⁶ Such outreach, however, should not be construed as providing the facility with a de facto “safe harbor” from enforcement for past regulatory failures.