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March 26, 2020

Ms. Vanessa Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-0609

Re: File No. SR-BOX-2019-19; Proposed Rule Change to Adopt Rules Governing the Trading of Equity Securities on the Exchange Through a Facility of the Exchange Known as the Boston Security Token Exchange LLC

Investors Exchange LLC (“IEX”) welcomes the opportunity to comment on the latest amendment (“February Proposal”) by BOX Exchange LLC (“BOX”) to its Proposed Rule Change to Adopt Rules Governing the Trading of Equity Securities on the Exchange Through a Facility of the Exchange Known as the Boston Security Token Exchange LLC.¹

BOX is in effect applying to become the 16th national securities exchange for the trading of NMS stocks.² IEX believes that the February Proposal leaves unanswered many critical questions about the effect on market competition, investor protection, and market efficiency. Accordingly, we believe the present record does not provide a basis for a determination by the Commission that the February Proposal is consistent with the standards of the Securities Exchange Act of 1934 (“Exchange Act”). We raise some of these questions in this letter.

Most notably, BOX had stated in a previous amendment that, in its view, Rule 12f-5 under the Exchange Act would require other exchanges to invest in special-purpose infrastructure in order to trade BSTX-listed securities. IEX is concerned that this may impose an unreasonable burden on competition and generally violate the spirit of the National Market System.

In addition, we believe that the Commission should extend the period for public comment by extending the time for action by 60 days beyond the current deadline, which is March 27, 2020. In light of recent market volatility and the need to focus on addressing effects of the coronavirus pandemic, IEX does not

¹ Securities Exchange Act Release No. 34-88300, File No. SR-BOX-2019-19 (February 28, 2020), 85 FR 13242 (March 6, 2020)

² Or 17th, see MIAX PEARL’s Proposed Rule Change to Adopt Rules Governing the Trading of Equity Securities, Release No. 34-88132, File No. SR-PEARL-2020-03



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believe industry members or investors have had a reasonable chance to evaluate the February Proposal and whether and how it addresses concerns raised to previous iterations of the proposal.

Description of the February Proposal

In the February Proposal, BOX applied for BSTX to become a listing exchange for NMS stocks with listing standards substantially similar to those of NYSE American. Custody, clearance and settlement would follow standard procedures through DTC and NSCC.

A central differentiating feature of BSTX would be the existence of a secondary recordkeeping mechanism based on the Ethereum public blockchain (“Secondary Recordkeeping Mechanism”). The data reflected in the Secondary Recordkeeping Mechanism would be a subset of the ownership records maintained by DTC and would be purely informative. BSTX Participants – BOX members that would elect to trade on BSTX – would have to report their end-of-day positions in BSTX-listed stocks to BSTX. BSTX would then update the Secondary Recordkeeping Mechanism through external service providers (“Wallet Managers”). Some market participants who are not BSTX Participants may not report their end-of-day positions: the net missing balance would be attributed to a generic account on the Secondary Recordkeeping Mechanism (“Omnibus Wallet”).

In BOX’s terminology, a “Security Token” essentially means a BSTX-listed NMS stock. In particular, a “Security Token” is not an Ethereum token, or any other type of digital asset commonly referred to as a token. However, the Secondary Recordkeeping Mechanism would presumably use tokens, in the usual digital asset sense. We will refer to those as “SRM tokens” for the purpose of this letter.

Rule filing history leading up to the February Proposal

On May 30, 2019, BOX submitted an initial BSTX Proposal under File No. SR-BOX-2019-19 (“May Proposal”).³ In it, BOX envisioned BSTX as a “no-UTP, no OTC” exchange:

The Exchange proposes to limit trading in security tokens to BSTX only in order to concentrate liquidity in security tokens on a single trading center. [...] Specifically, to limit over-the-counter (“OTC”) trading in security tokens, the Exchange is requesting that the Commission exercise its exemptive authority pursuant to Section 11A(c)(3) and Section 36(a) of the Exchange Act, to exempt the Exchange from Rules 19c-1 and 19c-3 under the Exchange Act, which generally

³ See <https://www.crowdfundinsider.com/2019/06/148013-boston-security-token-exchange-tzero-partner-box-exchange-files-proposed-rule-change-as-it-pushes-to-trade-digital-assets/>. The full May Proposal is available at <https://www.crowdfundinsider.com/wp-content/uploads/2019/06/SEC-Box-Exchange-Proposed-Rule-Change-SR-BOX-2019-19.pdf>



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prohibit the rules of a national securities exchange from limiting the ability of its members from trading securities otherwise than on an exchange. To limit trading in security tokens on other national securities exchanges, the Exchange is requesting that the Commission exercise its exemptive authority pursuant to Section 36(a) of the Exchange Act to exempt security tokens that are listed on BSTX from Section 12(f)(1)(A)(i) of the Exchange Act, which generally allows any national securities exchange to extend unlisted trading privileges to any security that is listed and registered on a national securities exchange.⁴

The May Proposal was not published by the SEC.

On September 27, 2019, BOX submitted a modified BSTX Proposal which was published by the Commission (“September Proposal”).⁵ The September Proposal did not seek a full exemption from unlisted trading privileges (“UTP”) but did restrict the ability of other exchanges to trade BSTX-listed stocks, in that other exchanges would have to develop specific infrastructure to adhere to the Secondary Recordkeeping Mechanism. Specifically, BOX expressed the view that Rule 12f-5 under the Exchange Act would require exchanges to adopt rules such that the exchange and its members would implement and use the Secondary Recordkeeping Mechanism in an appropriate way. Further, the September Proposal sought to restrict off-exchange trading in two ways. First, for an initial pilot period of one year, all market participants would have to report end-of-day positions to the Secondary Recordkeeping Mechanism. Second, after the initial pilot period of one year, market participants that are FINRA members would have to permanently report end-of-day ownership to the Secondary Recordkeeping Mechanism (under a FINRA rule yet to be proposed and approved).

On December 24, 2019, BOX submitted an Amendment to the September Proposal (“December Amendment”).⁶ Among other things, the December Amendment dropped the pilot period requirement and deleted language regarding a potential future FINRA rule requiring FINRA members to report end-of-day ownership to the Secondary Recordkeeping Mechanism.

On January 16, 2020, the Commission noticed the December Amendment and instituted proceedings to determine whether to approve or disapprove the proposed rule change (“January Order”).⁷

⁴ May Proposal, pp. 19-21, footnotes omitted

⁵ Release 34-87287, File No. SR-BOX-2019-19

⁶ https://lynxstorageaccount.blob.core.windows.net/boxvr/SE_resources/SR-BOX-2019-19_Amendment_1.pdf

⁷ Release No. 34-88002, File No. SR-BOX-2019-19



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Questions and Concerns

Effect on Competition

In its January Order and referring to BOX's September Proposal, the Commission asks:

Do commenters agree with the Exchange's assertion that the burden on another exchange of adopting additional rules to extend unlisted trading privileges to trade BSTX-listed security tokens is no different than the burden on an exchange that only trades equities having to first adopt rules to govern options trading prior to offering trading in options?

IEX disagrees with that assertion. Regulation NMS clearly envisions two types of NMS Securities: stocks and options. A well-established standard market infrastructure backs the trading of these two types of NMS Securities. The existence of this common market infrastructure means that trading venues can reasonably compete in the trading of either stocks or options. The burden on competition created by a security that necessitates special-purpose infrastructure is not comparable to that created by standard stocks or options.

In the February Proposal's Statement on Burden on Competition, BOX states:

[R]egarding other exchanges extending unlisted trading privileges to security tokens, the Exchange does not believe that the proposed Rules would impose a burden on competition that is not necessary or appropriate in furtherance of the purposes of the Exchange Act. Security tokens would trade, clear, and settle in the same manner as other NMS stock. Accordingly, other exchanges would be able to extend unlisted trading privileges to security tokens in accordance with Commission rules.

If other exchanges would no longer be expected to accommodate the Secondary Recordkeeping Mechanism, then this change does not appear to be reflected in changes to BSTX's proposed rules. Accordingly, IEX believes that BOX should be required to clearly address the following questions:

- (1) Does BOX believe that "Rule 12f-5 under the Exchange Act imposes the burden on exchanges" to have "rules in place that would require their members to obtain a whitelisted wallet address and to report their end-of-day security token balances in some manner so as to facilitate updates to the Ethereum blockchain as an ancillary recordkeeping mechanism" (as stated in the September Proposal)?
- (2) If the answer to (1) is no, how, if at all, is this reflected in BSTX rules as amended by the February Proposal, or has BOX simply changed its interpretation of Rule 12f-5? If the latter, what motivated the change in interpretation?



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- (3) What guarantees do market participants (including other national securities exchanges) have that BOX will not seek to limit UTP trading in BSTX-listed stocks in the future, for example based on an interpretation of Rule 12f-5 under the Exchange Act as reflected by the September Proposal?

The Potential for Confusion

Further, IEX does not believe BOX has sufficiently addressed the potential for confusion by investors and other participants because of a discrepancy between DTC ownership records and records maintained through the Secondary Recordkeeping Mechanism. In particular, BOX should be required to address the following questions:

- (4) In BOX's views, is there some "best-effort" threshold around inaccurate and/or partial secondary records of stock ownership that would sufficiently address investor confusion risk? What is the threshold?
- (5) Does the February Proposal meet this threshold?

Other Questions

Finally, without exhausting all the other questions that may be raised with more time to review the February Proposal, we believe that BOX should address the following additional questions:⁸

- (6) What is the purpose of the Secondary Recordkeeping Mechanism? Does it serve any purpose today? If the purpose is to "introduce blockchain technology in a gradual way" (February Proposal), with the belief that "[blockchain] technology may be able to help perfect the mechanism of a free and open market and a national market system" (February Proposal), what are the next steps, and what specifically will the eventual purpose of the Secondary Recordkeeping Mechanism be?
- (7) Has any registered broker-dealer that is currently a member of a national securities exchange that trades NMS stocks indicated its intention to become a BSTX Participant?
- (8) Why does BSTX act as an intermediary between BSTX Participants and Wallet Managers in the reporting of end-of-day positions? Why not direct reporting from BSTX Participants to Wallet Managers? What are the implications in terms of burden on competition for other exchanges who would like to extend UTP to BSTX-listed stocks?
- (9) What type of information will be publicly observable from the Secondary Recordkeeping Mechanism? For example, will the public be able to track the daily amount of stocks owned by a given BSTX Participant in its (anonymous) wallet? Will BSTX Participants be allowed to use multiple wallets and/or change wallets over time, for example in an effort to limit the public's ability to track their positions?

⁸ We also agree with the concerns identified in the Letter from Holly R. Smith, Eversheds Sutherland (US) LLP to J. Matthew DeLesDernier, Assistant Secretary, SEC, dated February 12, 2020. These concerns have not been fully or clearly addressed by the February Proposal.



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- (10) Would end-of-day positions reported to the Secondary Recordkeeping Mechanism reflect the most recent transactions (for example, same-day transactions), or would they match DTC's records, including any reporting lags related to the T+2 settlement cycle?
- (11) How would short positions be reflected in the Secondary Recordkeeping Mechanism?
- (12) How would the Secondary Recordkeeping Mechanism impact the locate process, clearing, settling or any other aspect of short sales?
- (13) Is there any mechanism to ensure that the positions reported by a BSTX Participant accurately match DTC's records? Would surveillance of the rule that requires a BSTX Participant to accurately report its positions be done by BSTX, or by FINRA pursuant to the Regulatory Services Agreement in place between BSTX and FINRA? In either case, what procedures would be used for surveillance and enforcement of that rule?
- (14) How would the Secondary Recordkeeping Mechanism handle overreporting of ownership balances? Would the total number of SRM tokens for a given BSTX stock fluctuate from one day to the next, with extra SRM tokens being created in overreported days, and then destroyed in the next non-overreported day?
- (15) Does the "Security Token" terminology, which refers to a BSTX-listed stock, create a risk of confusion with the SRM tokens used in the Secondary Reporting Mechanism?
- (16) Is BOX still working "*on adoption of a rule(s) by FINRA that would require FINRA members to obtain a wallet address and for end-of-day security token balance reports to be reported in a manner that would facilitate updates to the Ethereum blockchain to reflect ancillary records of security token ownership*" (as described in the September Proposal)?
- (17) Under which circumstances would a BSTX-listed stock qualify as a "*penny stock*" and what specifically are the "*additional regulation(s)*" it would then be subject to (see footnote 283 of the February Proposal)?

Conclusion

IEX supports marketplace innovation, but we believe BOX's proposal leaves many unanswered questions that must be addressed, including its impact on UTP and intermarket competition, and the potential for confusion relating to record ownership. We also believe that, in the current environment, market participants need more time to consider the proposal, based on the answers to these questions.

Sincerely,

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