



September 17, 2020

Via Electronic Mail

Vanessa Countryman
Secretary
U.S. Securities and Exchange Commission
100 F. Street, N.E.
Washington, D.C. 20549-1090

Re: File No. SR-BOX-2020-14

Dear Ms. Countryman:

BOX Exchange LLC (the “Exchange”) is responding to the recently submitted comment letter by the Securities Industry and Financial Markets Association (“SIFMA”)¹ on the above-referenced proposed rule change that would establish a rulebook for the Boston Security Token Exchange (“BSTX”) as a new facility of the Exchange (the “Proposal”).² In its recent Amendment No. 1, the Exchange amended the Proposal to, among other things, (i) eliminate the proposed use of T+1 as the standard settlement cycle for trades occurring on BSTX so that trades will instead settle on a T+2 basis, (ii) change the name of BSTX-listed securities from “security token” to “Securities” and (iii) provide clarifying guidance regarding certain aspects of the Proposal, including in response to certain questions and comments from SIFMA. The change from T+1 to T+2 was done in part in response to comments received from SIFMA and others.

The Exchange believes blockchain technology is capable of providing greater efficiency, security and other benefits to investors than currently exists and that consequently, over time, this technology will become ubiquitous in the financial markets. The reasons for this are addressed in the Proposal.³ Only the most basic elements and benefits of blockchain technology are included in the current Proposal. The Proposal represents an incremental change that will harmoniously incorporate blockchain technology with existing equity market infrastructure and regulations.

As previously noted by the Exchange in the comment file, the Exchange hosted two separate hour-long meetings with SIFMA members to answer questions regarding the Proposal on January 10, 2020 and March 20, 2020. Since then, the Exchange has also conducted

¹ See Letter from Ellen Green, Managing Director, Equities & Options Market Structure, SIFMA and Thomas F. Price, Managing Director, Operations, Technology, Cyber & BCP, SIFMA, to Vanessa Countryman, Secretary, Commission, re: File No. SR-BOX-2020-14 (Sep. 10, 2020) (“Letter”).

² See Securities Exchange Act Release No. 88946 (May 26, 2020), 85 FR 33454 (June 1, 2020). On August 12, 2020, the Commission published notice of the filing of Amendment No. 1 to the Proposal (“Amendment No. 1”). See Securities Exchange Act Release No. 89536 (Aug. 12, 2020), 85 FR 51250 (Aug 19, 2020).

³ Amendment No. 1 at 51262.

additional discussions about the Proposal with SIFMA representatives. It is concerning that despite these continued efforts by the Exchange to discuss the Proposal with SIFMA and its members, SIFMA does not acknowledge these efforts in its Letter and no SIFMA member firm has stepped forward in the comment process to identify itself and associate its name and reputation with the concerns stated in the SIFMA comment letters. Because SIFMA has not said who the interested members are, it is impossible for the Exchange to know how many members hold the views expressed in the Letter and whether they may have business interests of their own that are potentially in competition with the Proposal. The Exchange notes that SIFMA again belatedly submitted its Letter after the close of the Commission’s comment period, which does not respect the Commission’s process or the Exchange’s time. While most of the Letter explains the history of how the Exchange has modified the Proposal to address commenters concerns, the few new issues raised by SIFMA in the Letter are discussed below followed by the Exchange’s response.

The Proposal Would Not Force Any Market Participant To Become A BSTX Participant

- *SIFMA Letter* – “. . . [I]t appears to SIFMA that the Securities’ ancillary recordkeeping obligations would serve as a potential impediment for other exchanges to trade the Securities pursuant to UTP. Other exchanges could, by virtue of the ancillary recordkeeping requirements, be hesitant to trade the Securities pursuant to UTP because they would not want to put their members in the position of having to grapple with whether they might have obligations related to the Securities’ ancillary recordkeeping requirements. For instance, it is not clear from the Proposal whether a firm that is a member of other exchanges and is forced to become a BSTX Participant due to its clearing business would be subject to BSTX’s ancillary recordkeeping obligations in connection with effecting or clearing trades in Securities that are trading on one of those other exchanges pursuant to UTP. The mere fact that other exchanges and their member firms would need to grapple with issues could serve as an impediment for the other exchanges to trade the Securities pursuant to UTP.”⁴ SIFMA also states, “. . . in some instances there are certain firms that by virtue of the business they conduct may need to become BSTX Participants even if they would choose otherwise. For instance, certain firms that act as order consolidators for other firms may need to become BSTX Participants if customers of such other firms trade BSTX’s Securities.”⁵

Contrary to SIFMA’s unsubstantiated assertions, no market participant would be forced by the Proposal to become a BSTX Participant – whether by operating as a carrying firm, an order consolidator or otherwise. The only potential circumstance in which a firm would have to execute a trade in a Security at BSTX by virtue of the Commission’s Order Protection Rule under Regulation NMS⁶ would be if BSTX had a protected quotation and the firm wanted to

⁴ Letter at 5. Similarly, SIFMA claims that “certain firms . . . may need to become Participants if customers of such other firms trade BSTX’s Securities.” The Letter also references costs of the Proposal. *See Id* at 4-5.

⁵ *Id.*

⁶ 17 CFR 242.611.



trade through that protected quotation on an away market. But even in this circumstance, the firm could choose to execute the trade through a BSTX Participant at BSTX rather than becoming a BSTX Participant itself. This is exactly the same structure and choice for any firm as exists today. In the case of a firm that acts as a routing broker that nonetheless chooses to become a BSTX Participant, such a firm would be acting on an agency basis and therefore would not have an end-of-day balance in Securities arising from this routing broker-dealer function. Accordingly, reporting a zero end-of-day balance to the Exchange would not be burdensome.

In the event other markets eventually extend unlisted trading privileges to Securities, SIFMA says that it is unclear whether a market participant that trades Securities on multiple exchanges would be subject to BSTX's ancillary recordkeeping obligations in connection with effecting or clearing trades in Securities that are trading on one of the other exchanges. The Exchange has thoroughly addressed this issue already in the Proposal. The obligation on a BSTX Participant would be to report its end-of-day balance at DTC or such BSTX Participant's carrying firm in the relevant Security, pursuant to proposed Rule 17020(b).

- *From the Proposal* – “To update the Ethereum blockchain to reflect ownership of Securities as an ancillary recordkeeping mechanism, the Exchange proposes to require that each BSTX Participant, either directly or through its carrying firm, report each business day to BSTX **certain end-of-day Security balances** in a manner and form acceptable to BSTX.”⁷ [emphasis added.]

For avoidance of doubt, BSTX Participants under the Proposal will not be subject to reporting in connection with effecting or clearing trades in Securities.⁸

The Ancillary Recordkeeping Function Has A Clearly Defined Regulatory Objective

- *SIFMA Letter* – “. . . BOX further asserts that the ancillary recordkeeping obligations are no different than other reporting obligations that have been imposed on member firms such as the large option position reporting (“LOPR”) requirements adopted by the options exchanges and FINRA that obligate firms to report large options positions at the end of the day to the exchanges and FINRA. In response, SIFMA notes that the LOPR obligation is a regulatory requirement designed to help regulators monitor for market manipulation by requiring the reporting of large options positions by firms. The proposed BSTX ancillary recordkeeping obligations, however, are not related to any regulatory objectives.”⁹

⁷ Amendment No. 1 at 51258.

⁸ See e.g. Amendment No. 1 at 51252 (stating “Securities would meet the definition of NMS stocks and would trade, clear, and settle in the same manner as all other NMS stocks traded today. . . In this way, Securities are entirely compatible with the existing NMS structure, with one additional reporting and recordkeeping component specific to BSTX Participants. As described in further detail below, the ancillary recordkeeping process would in no way modify or alter market participants’ obligations under Regulation NMS.”).

⁹ Letter at 5.

BOX disagrees with SIFMA’s unsupported assertion that the proposed ancillary recordkeeping function is not related to any regulatory objectives. The Exchange has addressed this directly in the Proposal already and states the following:

- *From the Proposal* – “[T]he Exchange believes that the requirements regarding the ancillary recordkeeping process will promote the use of the functionality of smart contracts and their ability to allocate and re-allocate Security balances using [blockchain technology] across multiple addresses in connection with end-of-day Security position balance information of BSTX Participants such that the requirements will allow market participants to observe and increase their familiarity with the capabilities and potential benefits of blockchain technology in a context that parallels current equity market infrastructure and thereby advances and protects the public’s interest in the use and development of new data processing techniques that may create opportunities for more efficient, effective and safe securities markets.”¹⁰

The Proposal is Consistent With Exchange Act Sections 6(b)(5) And 17(A)

- *SIFMA Letter* – “SIFMA continues to believe that the Proposal contains novel aspects related to the current clearance, settlement and related recordkeeping processes for equity securities that are potentially inconsistent with the Exchange Act. Specifically, Section 6(b)(5) of the Exchange Act requires the rules of an exchange, ‘to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities.’ Similarly, Section 17A(a) of the Exchange Act requires the Commission to facilitate a national system for the clearance and settlement of securities transactions consistent with certain Congressional findings including the finding that ‘the development of uniform standards and procedures for clearance and settlement will reduce unnecessary costs and increase the protection of investors and persons facilitating transactions by and acting on behalf of investors.’ By creating unique recordkeeping requirements that only apply to the Securities, SIFMA believes that the Proposal’s ancillary recordkeeping obligations are potentially inconsistent with these Exchange Act requirements.”¹¹

SIFMA correctly acknowledges in the Letter that trades in Securities would be cleared and settled through NSCC and DTC just like other exchange-traded equity securities today. In fact, the Exchange has already completed its testing work with NSCC to facilitate this process. Accordingly, the Proposal is entirely consistent with Congress’ finding in Section 17A of the Exchange Act that “the development of uniform standards and procedures for clearance and settlement will reduce unnecessary costs and increase the protection of investors and persons facilitating transactions by acting on behalf of investors.” SIFMA’s assertion that the Proposal is inconsistent with this finding is inconsistent with SIFMA’s own acknowledgement in the Letter of how trades in Securities will be cleared and settled. The Exchange notes that the proposed

¹⁰ Amendment No. 1 at 51263.

¹¹ Letter at 3.



ancillary recordkeeping process for end-of-day balances regarding Securities is separate from the clearance and settlement process. Regarding Section 6(b)(5), the Exchange explains in numerous instances throughout the Proposal why the Proposal is consistent with this Section of the Exchange Act. In this regard, the Exchange directs SIFMA and members of the public to the detailed analysis found on pages 51257; 51260 (at footnote 86); 51261; 51269; 51272; 51273; 51274; 51275; 51277; 51278; 51279; 51280; 51282; 51283; 51287 and 51290 of the Federal Register version of the Proposal.

The Proposal Applies Only To BSTX Participants, Has Been Adjusted As A Result Of Public Comments, And Costs For Firms Choosing to Be BSTX Participants Are Minimal

- *SIFMA Letter* – “SIFMA previously expressed concerns regarding the ancillary recordkeeping aspect of the Proposal. We commented that the Proposal does not explore in sufficient detail the costs or other impacts on firms associated with adopting systems to accommodate the infrastructure needed to manage the security tokens’ distributed ledger technology, including establishing wallets and associated recordkeeping. In addition, we commented that in response to concerns about how other exchanges might trade the Securities pursuant to unlisted trading privileges (“UTP”) and whether they might be required to adopt BOX’s proprietary technology if they choose to do so, BOX asserted that such other exchanges are not obligated to adopt BOX’s technology and are free to adopt other forms of distributed ledger technology to track equity ownership on an ancillary basis. We further commented that having exchanges adopt different forms of distributed ledger technology to track ownership of equity securities could cause additional costs to the industry.”¹²

SIFMA states, again, that it is concerned about the Proposal because it is made by single exchange without actively working with and soliciting input from the industry. The Exchange notes that the notice and public comment process under the Exchange Act is the mechanism for soliciting comments on proposals by self-regulatory organizations. The Exchange has submitted the proposal twice, discussed the proposal with representatives from SIFMA and member firms on at least three separate occasions, and, as acknowledged by SIFMA in its Letter, already modified the Proposal in part based on comments from SIFMA to move to a T+2 settlement cycle. If this is not actively working with and soliciting input from the industry, it is hard to imagine what is.¹³

Regarding the costs associated with the ancillary recordkeeping process, the Exchange maintains the views expressed in the Proposal. As the Proposal states, “The Exchange does not believe that imposing the end-of-day Security reporting requirement on BSTX Participants is unfairly discriminatory or burdens competition because all market participants are free to choose whether to become a BSTX Participant or not and there is no limitation imposed by the

¹² *Id.* at 5-6.

¹³ Regarding SIFMA’s concerns about “how other exchanges might trade the Securities pursuant to UTP,” the Exchange notes that no comments have been submitted by any national securities exchange following the modifications included in Amendment No. 1.



Exchange on the ability to trade Securities on other markets. Market participants that voluntarily choose to become BSTX Participants must comply with the rules of the Exchange, but they remain free to become a member of another exchange that supports trading of Securities or to purchase the Securities over the counter. The Exchange further notes that it believes the end-of-day Security balance reporting process would not impose a substantial burden on BSTX Participants, because it would not require significant resources or time.”¹⁴ SIFMA does not present any supporting information in its Letter to back its claim that these costs would be substantial.

For market participants that choose to become BSTX Participants, the ancillary recordkeeping process will not require a significant commitment of resources. As stated in the Proposal, “A market participant that chooses to become a BSTX Participant would only need to obtain a wallet address from the Exchange and comply with the end-of-day Security balance reporting requirement pursuant to proposed Rule 17020. There is no technological investment needed by BSTX Participants under the proposal related to the use of distributed ledger technology.”¹⁵ The Exchange notes that the time and costs associated with obtaining a wallet address and DTC account balance information are not substantial.

The Exchange recognizes SIFMA’s assertion that its Proposal may require market participants that wish to become BSTX Participants to bear certain costs.¹⁶ The Exchange notes that there are always costs for market participants who choose to join a new exchange. However, as stated above, the Exchange believes that it is incorrect that the costs related to end-of-day reporting will be significant and notes that the Exchange has no commercial interest in imposing costs and burdens that would deter interest in the Proposal. However, even if one were to assume, for the sake of argument, that SIFMA’s assumptions regarding costs were correct, the Exchange notes that the arguments made in SIFMA’s Letter do not provide a legal basis on which the Proposal could be disapproved under the Exchange Act. Simply because market participants might not want to take on the additional operational processes and minimal costs associated with end-of-day reporting does not make the Proposal inconsistent with the Exchange Act. As explained throughout Amendment No. 1, the Proposal is consistent with the Exchange Act, including in relation BSTX Participants’ obligations regarding end-of-day reporting.¹⁷

Finally, the Exchange again notes that its Proposal represents an incremental change to incorporate blockchain technology within the current infrastructure and regulations for the equities market – including clearance and settlement of Securities through NSCC and DTC. It is difficult to imagine how any blockchain-related proposal could pose less disruption to existing equity market infrastructure and regulation. As the Exchange has noted, the Proposal will apply only to BSTX Participants. It is bounded by its terms, and any future structural changes would

¹⁴ Amendment No. 1 at 51262.

¹⁵ *Id.* at 51263.

¹⁶ *See e.g.* Letter at 4.

¹⁷ *See e.g., supra* note 12.



be subject to the Commission's rule filing process under Section 19 of the Exchange Act and public notice and comment.¹⁸ Disapproval would set an inappropriate standard of trade organizations being able to defeat innovative proposals under the Exchange Act simply because they do not like change. And it would be even more disappointing if the lack of transparency in the comment process to date was being used to try to undermine the Proposal for the benefit of unknown potential competitors.

* * *

The Exchange once again appreciates the opportunity to respond to commenters on the Proposal. The Exchange firmly believes that the Proposal is consistent with the requirements of the Exchange Act and must therefore be approved.

Please feel free to contact us with us with any questions at (617) 235-2400.

Sincerely,

A handwritten signature in black ink that reads "L. J. Fall". The signature is written in a cursive, slightly stylized font.

Lisa J. Fall
President
BOX Exchange LLC

¹⁸ See Letter from Lisa Fall, President, BOX Exchange LLC, to Vanessa Countryman, Secretary, Commission, re: File No. SR-BOX-2019-19 (Apr. 27, 2020).