

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-75766; File No. SR-BOX-2015-22)

August 27, 2015

Self-Regulatory Organizations; BOX Options Exchange LLC; Order Granting Approval of a Proposed Rule Change to Implement the Governance Provisions of an Equity Rights Program

I. Introduction

On June 25, 2015, BOX Options Exchange LLC (the “Exchange”) filed with the Securities and Exchange Commission (“Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> a proposed rule change to implement the governance provisions of a volume performance rights program (the “VPR Program”). The proposed rule change was published for comment in the Federal Register on July 13, 2015.<sup>3</sup> The Commission received no comments on the proposal. This order approves the proposed rule change.

II. Description

Under the VPR Program, BOX<sup>4</sup> Options Participants<sup>5</sup> (“Participants”) that take part in the Program will have the right to acquire equity in, and receive distributions from, BOX Holdings Group LLC (“Holdings”), an affiliate of the Exchange and direct parent entity of BOX, in exchange for a nominal cash payment and the achievement of certain order flow volume

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> See Securities Exchange Act Release No. 75374 (July 7, 2015), 80 FR 40100 (SR-BOX-2015-22) (“Notice”).

<sup>4</sup> “BOX” means BOX Market LLC, an options trading facility of the Exchange. See BOX Rule 100(a)(7).

<sup>5</sup> “Options Participant” or “Participant” means a firm, or organization that is registered with the Exchange pursuant to the Rule 2000 Series for purposes of participating in options trading on BOX as an “Order Flow Provider” or “Market Maker.” See BOX Rule 100(a)(40).

commitments over a period of five years.<sup>6</sup> Pursuant to the VPR Program, Volume Performance Rights (“VPRs”) were issued to Participants that elected to participate, met the eligibility criteria and made the initial cash payment (“Subscribers”).<sup>7</sup>

Each VPR is comprised of the right to receive 8.5 unvested new Class C Membership Units of Holdings (“Class C Units”), upon effectiveness of this proposed rule change. One VPR per Tranche will be eligible to vest each quarter of the five (5) year Program period, subject to the Subscriber meeting its volume commitment for that quarter. In addition, VPRs may be reallocated among Subscribers based upon exceeding or failing to meet Subscribers’ volume commitments during the VPR Program period.<sup>8</sup>

A. Ownership Units

As described in more detail in the Notice,<sup>9</sup> in order to implement certain aspects of the VPR Program, Holdings would amend its existing Limited Liability Company Agreement (the “Holdings LLC Agreement”) by adopting an Amended and Restated Limited Liability Company Agreement of Holdings (the “Restated Holdings LLC Agreement”), to create Class

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<sup>6</sup> See Securities Exchange Act Release No. 74114 (January 22, 2015), 80 FR 4611 (January 28, 2015) (SR-BOX-2015-03) (the “VPR Filing”). See also Securities Exchange Act Release No. 74171 (January 29, 2015), 80 FR 6153 (February 4, 2015) (SR-BOX-2015-05) (extending the deadline to participate in the VPR program until January 14, 2015) (the “Second VPR Filing”).

<sup>7</sup> See Notice, supra note 3, at 40101. The VPRs were issued in tranches of twenty (20) VPRs (each, a “Tranche”) with a minimum subscription of two (2) Tranches per Subscriber. According to the Exchange, twenty-seven (27) Tranches have been issued in connection with the VPR Program. See id.

<sup>8</sup> See Notice, supra note 3, at 40101.

<sup>9</sup> See id.

C Units.<sup>10</sup> Once Class C Units are created, Holdings will admit the Subscribers as Class C Members.<sup>11</sup>

The existing limitations on the percentage ownership of Holdings by Participants will continue to apply. Specifically, in the event that a Member, or any Related Person<sup>12</sup> of a Member, is a Participant, and the Member owns more than 20% of the Units,<sup>13</sup> alone or together with any Related Person of the Member (Units owned in excess of 20% being referred to as “Excess Units”), the Member and its designated Directors<sup>14</sup> will have no voting rights with respect to the Excess Units on any action relating to Holdings nor will the Member or its designated Directors, if any, be entitled to give any proxy with respect to the Excess Units in relation to a vote of the Members; provided, however, that whether or not the Member or its designated Directors, if any, otherwise participates in a meeting in person or by proxy, the Member’s Excess Units will be counted for quorum purposes and will be voted by the person presiding over quorum and vote matters in the same proportion as the Units held by the other Members are voted (including any abstentions from voting).<sup>15</sup>

Upon completion of the VPR Program, all outstanding Class C Units associated with vested VPRs will be automatically converted into an equal number of Class A Units and all outstanding Class C Units associated with unvested VPRs will be automatically cancelled and

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<sup>10</sup> See Notice, supra note 3 at, 40100. Currently, Holdings only has issued and outstanding Class A and Class B membership Units. See id. at 40101.

<sup>11</sup> See id.

<sup>12</sup> The Exchange is not proposing to change the definition of “Related Person.” See Notice, supra note 3, at 40101, n.9.

<sup>13</sup> “Units” means Class A Membership Units, Class B Membership Units and Class C Units of Holdings. See proposed Restated Holdings LLC Agreement Section 1.1 (defining “Units”).

<sup>14</sup> See proposed Restated Holdings LLC Agreement Section 4.1(a) (defining “Directors”).

<sup>15</sup> See proposed Restated Holdings LLC Agreement Section 7.4(h).

be of no further effect. All rights related to Class C Units will terminate automatically upon cancellation or conversion and rights related to the converted Class A Units will remain, subject to the terms of the Restated Holdings LLC Agreement.<sup>16</sup>

B. Voting

Each Class C Member will have the right to vote its Class C Units that are associated with vested VPRs (“Voting Class C Units”) on matters submitted to a vote of all holders of Units. VPRs will vest in accordance with the vesting provisions of the VPR Program.<sup>17</sup>

Members holding Voting Class C Units will vote with Members holding all other classes of Units. Members holding Voting Units<sup>18</sup> will be entitled to vote together, as a single class, each with one vote per Voting Unit so held.<sup>19</sup> Issued and outstanding Class C Units that are not Voting Class C Units will not have voting rights. According to the Exchange, as a Subscriber meets or exceeds its volume commitments, its voting powers as a Class C Member of Holdings will increase.<sup>20</sup> Similarly, if a Subscriber does not meet its volume commitment, its voting powers will decrease.<sup>21</sup>

The Holdings LLC Agreement currently provides, and the Restated Holdings LLC Agreement will continue to provide, that any Director designated by either MX US 2, Inc. or IB Exchange Corp may effectively block certain actions of Holdings (the “Major Action Veto”). Under the Restated Holdings LLC Agreement, upon vesting of VPRs associated with

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<sup>16</sup> See proposed Restated Holdings LLC Agreement Section 2.5(e).

<sup>17</sup> See Notice, supra note 3. See also VPR Filing, supra note 6.

<sup>18</sup> “Voting Unit” means any Class A Unit, Class B Unit, or Voting Class C Unit. See proposed Restated Holdings LLC Agreement, Section 1.1.

<sup>19</sup> See proposed Restated Holdings LLC Agreement Section 4.13(a).

<sup>20</sup> See Notice, supra note 3, at 40102.

<sup>21</sup> See id.

Class C Units equal to at least 25% of the total outstanding Units, the Major Action Veto will automatically expire and be of no further effect. In addition, when the 25% threshold is met, the Restated Holdings LLC Agreement provides that Holdings and its Members will take all necessary action to amend the Limited Liability Company Agreement of BOX to eliminate the Major Action Veto provisions therein that are applicable to BOX and inure to the benefit of MX US 2, Inc. and IB Exchange Corp and to provide that the executive committee of BOX will be constituted in the same manner as the Executive Committee of Holdings.<sup>22</sup>

The Restated Holdings LLC Agreement includes a new supermajority voting requirement that Members holding at least 67% of all outstanding Voting Units must vote to approve certain actions (the “Supermajority Actions”) by Holdings.<sup>23</sup> The supermajority voting requirement, however, would not apply to certain of these Supermajority Actions,<sup>24</sup> to the extent otherwise required by the Exchange to fulfill its regulatory functions or responsibilities or to oversee the BOX Market as determined by the board of the Exchange.

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<sup>22</sup> See proposed Restated Holdings LLC Agreement Section 16.4.

<sup>23</sup> See proposed Restated Holdings LLC Agreement Section 4.13(b). For further details on these actions, see Notice, *supra* note 3, at 40102-03.

<sup>24</sup> See, e.g., proposed Restated Holdings LLC Agreement Section 4.13(b)(vi)-(viii), (x), (xii), and (xiii). These provisions are: (1) the issuance, by Holdings, of any additional equity interests in, or any securities exchangeable for or convertible into equity securities of, Holdings, subject to specified exceptions; (2) the issuance, by BOX, of any additional equity interests in, or any securities exchangeable for or convertible into equity securities of, BOX, except as otherwise provided in the Facility Agreement; (3) permitting BOX to operate the BOX Market utilizing any other regulatory services provider other than the Exchange; (4) making a fundamental change to the business model of BOX to be other than a for-profit business; (5) altering the provisions relating to the designation of Directors set forth in Restated Holdings LLC Agreement; and (6) altering or amending any of the Supermajority Actions provisions as set forth in the Restated Holdings LLC Agreement. *Id.*

C. Directors

The Exchange proposes to amend the Holdings LLC Agreement with respect to the composition of the Holdings Board. Currently, MX US 2, Inc. has the right to designate up to five (5) Directors, IB Exchange Corp has the right to designate up to two (2) Directors and each other Member has the right to designate one (1) Director to the Holdings Board and the Holdings Board has the power to increase the size of the Holdings Board and to authorize new Members to designate Directors.<sup>25</sup>

Under the Restated Holdings LLC Agreement, no Member may designate more than three (3) Directors and each Member may designate the maximum number of Directors permitted under any one (1) (but not more than one) of the following criteria: (i) each Member, so long as it (together with its respective Affiliates) holds a combined total of Class A Units and Class B Units greater than two and one-half percent (2.5%) of all outstanding Voting Units, will be entitled to designate one (1) Director, (ii) each Member, so long as it (together with its respective Affiliates) holds a combined total of Voting Class C Units greater than four percent (4%) of all outstanding Voting Units, will be entitled to designate one (1) Director, (iii) each Member, so long as it (together with its respective Affiliates) holds a combined total of Voting Units greater than fourteen percent (14%) of all outstanding Voting Units, will be entitled to designate two (2) Directors, (iv) each Member, so long as it (together with its respective Affiliates) holds a combined total of Voting Units greater than twenty-eight percent (28%) of all outstanding Voting Units, will be entitled to designate three (3) Directors, and (v) each other existing Member may designate one (1) Director.<sup>26</sup> Directors serving on the

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<sup>25</sup> See Notice, supra 3, at 40103.

<sup>26</sup> See proposed Restated Holdings LLC Agreement Section 4.1(a)(i)-(vi).

Holdings Board may also serve on the board of directors of any subsidiary of Holdings. If a Member ceases to qualify for the right to designate a Director then serving, then that Director will then automatically be removed from the Holdings Board.<sup>27</sup>

The Restated Holdings LLC Agreement also will amend the provisions governing the right of Members to designate members of the Executive Committee of Holdings (the “Executive Committee”), if any.<sup>28</sup> Currently, MX US 2, Inc. has the right to designate up to two (2) members of the Executive Committee (“EC Members”) and IB Exchange Corp has the right to designate one (1) EC Member. Under the Restated Holdings LLC Agreement, any Member with the right to designate three (3) Directors to the Holdings Board will have the right to designate up to two (2) EC Members and any Member with the right to designate two (2) Directors to the Holdings Board will have the right to designate one (1) EC Member.<sup>29</sup>

Subscribers will also have the right to designate one individual to a new Advisory Committee organized by Holdings, the purpose of which will be to advise and make recommendations to Holdings with respect to the Exchange’s competitiveness in the marketplace.<sup>30</sup> Only Subscribers will have the right to designate individuals to serve on the Advisory Committee.<sup>31</sup> The Advisory Committee will be advisory only and will not have any powers, votes or fiduciary duties to Holdings.<sup>32</sup>

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<sup>27</sup> See proposed Restated Holdings LLC Agreement Section 4.1(b).

<sup>28</sup> See Notice, supra note 3, at 40103.

<sup>29</sup> See proposed Restated Holdings LLC Agreement Section 4.2(c). Other provisions relating to the composition of the Executive Committee will be unchanged.

<sup>30</sup> See Notice, supra note 3, at 40103.

<sup>31</sup> See VPR Filing, supra note 6, at 4613.

<sup>32</sup> See Notice, supra note 3, at 40103.

D. Distributions

The Restated Holdings LLC Agreement provides that, once per year, Holdings will make a distribution (an “Annual Distribution”) to its Members to the extent funds are available for distribution.<sup>33</sup> In determining the amount of each Annual Distribution, the Holdings Board will first provide for any regulatory needs of BOX and the Exchange, as determined by the Exchange Board, and any Annual Distribution amounts will be calculated after taking into account all financial and regulatory needs of the Exchange, as determined by the Exchange.<sup>34</sup> The Annual Distribution will be equal to 80% of Free Cash Flow,<sup>35</sup> except as limited by applicable law, including for regulatory and compliance purposes. In addition, another 15% of Free Cash Flow will be included in the distribution, except to the extent the Holdings Board determines that any portion thereof is (i) required for the operations of Holdings and its subsidiaries, which will be reflected on the annual budget for the next year, (ii) required for payment of liabilities or expenses of Holdings, or (iii) required as a reserve to make reasonable provision to pay other claims and obligations then known to, or reasonably anticipated by, BOX or Holdings. When, as and if declared by the Holdings Board, Holdings will make the

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<sup>33</sup> See proposed Restated Holdings LLC Agreement Section 8.1. Distributions on Class C Units will not be paid until this proposed rule change is effective. Distributions payable on Class C Units that accrue before such effectiveness will be held in a segregated account until such effectiveness. If this rule filing does not become effective by July 1, 2016, a Subscriber may terminate its involvement in the VPR Program and any and all distributions with respect to Class C Units payable to that Subscriber held in the segregated account will be released back to Holdings and distributed to existing Members in accordance with the terms of the Holdings LLC Agreement. See Notice, supra note 3, at 40104, n.21. See also VPR Filing, supra note 6, at 4612, n.15.

<sup>34</sup> See proposed Restated Holdings LLC Agreement Section 8.1.

<sup>35</sup> “Free Cash Flow” means consolidated net income, plus depreciation, less capital expenditures (in each case calculated in accordance with generally accepted accounting principles in the United States, as in effect from time to time) of Holdings and BOX, for the calendar year. See proposed Restated Holdings LLC Agreement Section 1.1.



cash distribution to each Member pro rata in accordance with the number of Units held by each Member, which will be determined by multiplying the aggregate Annual Distribution amount by each Member's Percentage Interest<sup>36</sup> on the record date. Distributions to Class C Members may be adjusted as provided in the Members Agreement.<sup>37</sup>

### III. Discussion

The Commission has reviewed carefully the proposed rule change and finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.<sup>38</sup> In particular, the Commission finds that the proposed rule change is consistent with Sections 6(b)(1) of the Act,<sup>39</sup> which, among other things, requires a national securities exchange to be so organized and have the capacity to be able to carry out the purposes of the Act, and to enforce compliance by its members and persons associated with its members with the provisions of the Act, the rules and regulations thereunder, and the rules of the exchange. The Commission also finds that the proposal is consistent with Section 6(b)(5) of the Act,<sup>40</sup> which requires that the rules of the exchange be designed to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest.

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<sup>36</sup> "Percentage Interest" with respect to a Member means the ratio of the number of Units held by the Member to the total of all of the issued Units, expressed as a percentage and determined with respect to each class of Units, whenever applicable.

<sup>37</sup> See proposed Restated Holdings LLC Agreement Section 8.1 and see VPR Filing supra, note 6.

<sup>38</sup> In approving the proposed rule changes, the Commission has considered their impact on efficiency, competition and capital formation. See 15 U.S.C. 78c(f).

<sup>39</sup> 15 U.S.C. 78f(b)(1).

<sup>40</sup> 15 U.S.C. 78f(b)(5).

Although Holdings does not carry out any regulatory functions, all of its activities must be consistent with the Act. Holdings is the sole owner of BOX, which owns and operates the BOX options trading platform as a facility of the Exchange. As a facility of a national securities exchange, the options trading platform is not solely a commercial enterprise, but is an integral part of an SRO that is registered pursuant to the Act and therefore subject to obligations imposed by the Act. The Commission believes that the Restated Holdings LLC Agreement is reasonably designed to enable Holdings to operate in a manner that is consistent with this principle. In this regard, the Commission believes that the proposed changes related to the VPR Program will not impact provisions of Holding's corporate governance documents that were designed to enable the Exchange and BOX to operate in a manner that complies with the federal securities laws, and were intended to assist the Exchange in fulfilling its self-regulatory obligations and administering and complying with the requirements of the Act.<sup>41</sup> The Commission also believes that the proposed rule change will allow the Commission to continue to exercise its plenary regulatory authority over the Exchange and continue to provide the Commission and the Exchange with access to necessary information that will allow the Exchange to comply, and enforce compliance, with the Act.

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<sup>41</sup> See Securities Exchange Act Release No. 66871 (April 27, 2012), 77 FR 26323, 26329-30 (May 3, 2012) (describing provisions in governing documents designed to help maintain the independence of the regulatory functions of the Exchange, including, but not limited to, Section 4.12(a) of the proposed Restated Holdings LLC Agreement, which provides that each of the Members, Directors, Officers, employees and agents of Holdings shall give due regard to the preservation of the independence of the self-regulatory function of the Exchange and to its obligations to investors and the general public and shall not take actions which would interfere with the effectuation of decisions by the board of directors of the Exchange relating to its regulatory functions (including disciplinary matters) or which would interfere with the Exchange's ability to carry out its responsibilities under the Exchange Act, and Section 4.12(b), which provides that Holdings and its Members shall comply with the federal securities laws and the rules and regulations thereunder and shall cooperate with the Commission and the Exchange pursuant to and to the extent of their respective regulatory authority).

With respect to the Annual Distributions, the Commission notes the Exchange represents that before making any distribution to its Members, the Holdings Board will first provide for any regulatory needs of BOX and the Exchange (as determined by the Exchange Board).<sup>42</sup> The Commission believes that the requirement to first provide for the regulatory needs of BOX and the Exchange is designed to facilitate the ability of the Exchange to fulfill its regulatory obligations under the Act and help to ensure that the proposed provisions regarding distributions maintain the independence of the Exchange's regulatory function and would not be made in violation of the Exchange's legal and regulatory responsibilities. The Commission therefore believes that the proposed provisions in the Restated Holdings LLC Agreement related to distributions are consistent with the Act.

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<sup>42</sup> See Notice, supra note 3, at 40103 (“In determining the amount of each Annual Distribution, the Holdings Board will first provide for any regulatory needs of BOX and the Exchange, as determined by the Exchange Board, and any Annual Distribution amounts will be calculated after taking into account all financial and regulatory needs of the Exchange, as determined by the Exchange.”).

IV. Conclusion

For the foregoing reasons, the Commission finds that the proposed rule change is consistent with the Act and the rules and regulations thereunder applicable to a national securities exchange.

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act<sup>43</sup> that the proposed rule change (SR-BOX-2015-22) is approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>44</sup>

Robert W. Errett  
Deputy Secretary

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<sup>43</sup> 15 U.S.C. 78s(b)(2).

<sup>44</sup> 17 CFR 200.30-3(a)(12).