BOX® OPTIONS EXCHANGE

March 20, 2015

VIA FACSIMILE AND FEDERAL EXPRESS

Brent J. Fields
Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090

Re: SR-OCC-2015-02, Securities Exchange Act Release No. 74452
Petition for Review

Dear Mr. Fields,

Enclosed please find the original and three copies of the Petition for Review regarding the above-captioned matter. BOX Options Exchange LLC ("BOX") submits this Petition for Review. Pursuant to Rule 154(c) of the Securities and Exchange Commission's Rules of Practice, BOX certifies that the enclosed Petition for Review does not exceed 7,000 words. This Petition for Review was sent via facsimile telephone number 202-772-9324 and via Federal Express on March 20, 2015. Also enclosed, please find a Certificate of Service and a facsimile confirmation sheet.

Any questions concerning this matter can be directed to me at 617-235-2235.

Sincerely,

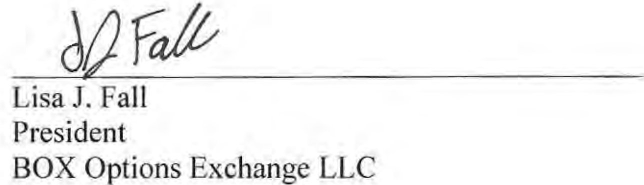
Lisa J. Fall
President
BOX Options Exchange LLC

CERTIFICATE OF SERVICE

I, Lisa J. Fall, President of BOX Options Exchange LLC, hereby certify that on March 20, 2015, I served copies of the attached Petition for Review of SR-OCC-2015-02, Exchange Release No. 74452, by way of facsimile and that the original was sent that day by Federal Express to:

Brent J. Fields
Secretary
Securities and Exchange Commission
100 F. Street N.E.
Washington, D.C. 20549-1090

James Brown
General Counsel
The Options Clearing Corporation
1 N. Wacker Drive, Suite 500
Chicago, IL 60606



March 20, 2015
Date

Lisa J. Fall
President
BOX Options Exchange LLC

TABLE OF CONTENTS

TABLE OF AUTHORITIES.. ii

PETITION FOR REVIEW..1

Preliminary Statement 1

Background and Description of the Filing 3

Applicable Legal Requirements 5

Significant Policy Concerns that Warrants Commission Consideration 6

Deficiencies in Staff's Approval of the Filing 8

A. The OCC Failed to Abide by its own By-Laws 8

B. Burden on Competition 13

CONCLUSION 16

TABLE OF AUTHORITIES

STATUTES

5 U.S.C. § 706(2)(A)..................... 3, 8

15 U.S.C. 78q-1(b)(3)(I)..................... 13

15 U.S.C. 78c(f)..................... 14

CASES

Business Roundtable v. Securities and Exchange Commission,
647 F.3d 1144 (D.C. Cir. 2011)..................... 3, 8

Chamber of Commerce v. Securities and Exchange Commission,
412 F.3d 133 (D.C. Cir. 2005)..................... 3, 8, 14

OTHER AUTHORITIES

Exchange Act Release No. 74452 (March 6, 2015),
80 FR 13058 (March 12, 2015)..................... 1, 9, 13, 14

Exchange Act Release No. 46257 (July 25, 2002),
67 FR 49729 (July 31, 2002)..................... 4, 8, 10, 15, 16

Exchange Act Release No. 46469 (September 6, 2002),
67 FR 58093 (September 13, 2002)..................... 4

OCC By-Laws, *available at:* http://optionsclearing.com/
components/docs/legal/rules_and_bylaws/occ_bylaws.pdf..................... 9, 12

OCC Charter, *available at:* http://www.optionsclearing.com/
components/docs/about/corporate-information/board_of_directors_charter.pdf..................... 11

OCC Board of Directors Corporate Governance Principles, *available at*
http://optionsclearing.com/components/docs/about/corporate-
information/board_corporate_governance_principles.pdf 12

RULES

17 CFR 201.430..................... 5

17 CFR 201.431..................... 5

17 CFR 201.411(b)(2)..................... 5

Before the
SECURITIES AND EXCHANGE COMMISSION

In the Matter of the Petition of:	)	File No. SR-OCC-2015-02
BOX Options Exchange LLC	)	

Petition for Review

BOX Options Exchange LLC ("BOX") hereby petitions for further review of an action taken by the Staff pursuant to delegated authority. Specifically, on March 6, 2015, the Division of Trading and Markets ("Staff") of the Securities and Exchange Commission issued an Order[1] approving the Options Clearing Corporation's ("OCC") proposal to raise additional capital from four shareholder exchanges and to pay dividends to these select exchanges (the "Capital Plan").

Preliminary Statement

The Capital Plan, as approved by the Staff, fundamentally alters the competitive nature of the options industry by providing the OCC's four owner exchanges[2] an excessive dividend in perpetuity. It is estimated that the dividend could potentially reach 20% per year in the first few years and in theory could go higher from there. This excessive dividend will act as a subsidy to the Shareholder Exchanges. The Approval Order drastically alters the competitive dynamic

[1] See Securities Exchange Act Release No. 74452 (March 6, 2015), 80 FR 13058 (March 12, 2015)(the "Approval Order").
[2] The owners of the OCC ("Shareholder Exchanges") are: Chicago Board Options Exchange, Incorporated ("CBOE"), International Securities Exchange ("ISE"), NASDAQ OMX PHLX LLC ("NASDAQ"), and NYSE MKT LLC and NYSE Arca, Inc. (collectively, "NYSE").

between the Shareholder Exchanges and the non-Shareholder Exchanges[3] by providing an unfair competitive advantage to the Shareholder Exchanges.

The Capital Plan raises numerous policy issues that should be addressed by the Commission, not by the Staff acting on delegated authority. These policy issues arise out of the unique nature of the OCC and more specifically, the monopoly status of the OCC, exchange ownership, lack of an over-the-counter market for options, and exchange veto power in certain situations. The Staff erred in not adequately analyzing the Capital Plan to take into account these unique factors.

The Staff also made numerous errors of fact and law while approving the Capital Plan. For example, the Staff incorrectly concluded that any burden on competition was not undue because it is necessary and appropriate in furtherance of the Act regardless of the level of the dividend. The Staff failed to adequately analyze the level of the dividend and the effect that it will have on competition. Further, throughout the Approval Order the Staff relied on the fact that the OCC's Board of Directors ("OCC's Board") approved the Capital Plan. In doing so, the Staff failed to take into account the unique nature of the OCC as a monopoly and the ownership structure where only four exchanges are owners of the OCC. This unique structure, coupled with the fact that the interested directors did not recuse themselves from the deliberations and vote on the Capital Plan, raises significant policy concerns that require careful consideration from the Commission.

[3] The non-Shareholder Exchanges are: BOX, BATS Global Markets, Inc. ("BATS"), and Miami International Securities Exchange, LLC ("MIAX"). There are four additional non-shareholder exchanges; however, all four are associated with a Shareholder Exchange and cannot therefore be considered non-Shareholder Exchanges with regard to this matter.

The governance process the OCC followed is extremely concerning. The OCC did not provide the non-Shareholder Exchanges with prompt notice of the Capital Plan as required by its own By-Laws. This notice would have given the non-Shareholder Exchanges the opportunity to make a presentation to the OCC's Board and possibly provide a more fair alternative to the OCC. Additionally, the directors representing the Shareholder Exchanges failed to recuse themselves from the deliberations or the vote regarding the Capital Plan even though the Shareholder Exchanges had a strong financial interest in the outcome. Further, the OCC's Board had public director vacancies when it voted to approve the Capital Plan. The presence of these disinterested directors is essential to having a fair process and the OCC's failure to eliminate the vacancies before the vote seriously taints the approval process.

One of the most troubling aspects of the Approval Order is that it contains virtually no substantive analysis of the competitive effects of the Capital Plan. The Staff makes no reference to any market studies, reviews, statistics, or economic analysis relating to how the Capital Plan would affect competition among options exchanges and fee structures and what the impact would be on investors. The Staff acted in an arbitrary and capricious manner and abused its discretion in approving the Capital Plan without engaging in or considering any such studies.[4]

Background and Description of the Filing

- Founded in 1973, the OCC is the largest clearing organization in the world for equity derivatives and is the sole clearing house for exchange-listed options in the

[4] See Administrative Procedure Act, 5 U.S.C. Sec. 706(2)(A) (authorizing courts to set aside agency action that is "arbitrary, capricious, and abuse of discretion or otherwise not in accordance with law"); *Business Roundtable v. Securities and Exchange Commission*, 647 F.3d 1144, 1148 (D.C. Cir. 2011)(holding that "the Commission acted arbitrarily and capriciously for having failed ... adequately to assess the economic effects of a new rule"); *Chamber of Commerce v. Securities and Exchange Commission*, 412 F.3d 133, 144 (D.C. Cir. 2005) (finding Commission violated its obligations under the APA because it failed in its "statutory obligation to do what it can to apprise itself – and hence the public and the Congress—of the economic consequences of a proposed regulation before it decides whether to adopt the measure.")

U.S. The U.S. Securities and Exchange Commission ("SEC") and the U.S. Commodity Futures Trading Commission have jurisdiction over the OCC. The U.S. options industry is different from the equities market in that there are no over-the-counter options markets, meaning that all transactions must occur on a registered national securities exchange and be cleared by the OCC. Although all transactions that occur on a registered national securities exchange are required to be cleared at the OCC, only four exchanges have equity ownership in the OCC. All exchanges are required to be OCC "participants," which historically meant equity ownership for exchanges formed prior to 2002, but meant becoming OCC noteholders for any exchanges formed after 2002. [5]

The OCC has always operated as a non-profit industry utility. This means the OCC set fees at a level intended to cover operating expenses and maintain a capital reserve. In past years, if the OCC collected fees in excess of its needs, the OCC would refund the excess to its clearing members. The OCC never used the excess to provide a dividend payment to the Shareholder Exchanges as doing so would have been unfair to non-Shareholders Exchanges.

In the Capital Plan, which was approved by the Staff, the OCC is proposing to amend its By-Laws and other governing documents, and to adopt certain policies, for the purpose of implementing the recapitalization under which the Shareholder Exchanges would make an additional capital contribution and commit to replenishment capital, and would receive, among other things, the right to receive dividends in perpetuity from the OCC. Due to the dividend payment to Shareholder Exchanges, the amount of any refunds to clearing members will be

[5] In 2002, the OCC removed the requirement in its By-Laws that all national securities exchanges for which t it clears transactions be owners of the OCC. See Securities Exchange Act Release No. 46257 (July 25, 2002), 67 FR 49729 (July 31, 2002)(SR-OCC-2002-02)("2002 Filing"). See also Securities Exchange Act Release No. 46469 (September 6, 2002), 67 FR 58093 (September 13, 2002)(Order Approving SR-OCC-2002-02).

reduced, and could be permanently eliminated under certain circumstances. The OCC has determined that its currently appropriate "Target Capital Requirement" is $247 million, reflecting a Baseline Capital Requirement of $117 million, which is equal to six months of projected operating expenses, plus a Target Capital Buffer of $130 million. As of December 31, 2013, the OCC had total shareholders' equity of approximately $25 million, meaning that the OCC needs to add additional capital of $222 million to meet its 2015 Target Capital Requirement.

Applicable Legal Requirements

Rules 430 and 431 of the Rules of Practice, 17 CFR 201.430 and 201.431, provide for Commission review of Staff action taken by delegated authority upon request by a person aggrieved by the Staff's action. BOX is a national securities exchange registered with the Commission and is directly and negatively affected by the Staff's approval of the Capital Plan because, as discussed in detail below, it drastically alters the landscape of the options industry and radically shifts the competitive balance between the Shareholder Exchanges that are owners of the OCC and the non-Shareholder Exchanges. BOX has complied with the procedural requirements contained in Rule 430.[6]

Rule 431 contains the requirements relating to the Commission's review of the petition. Rule 431 provides that the Commission, in determining whether to grant review in response to a petition such as this one, must look to the standards set forth in Rule 411(b)(2) of the Rules of Practice, 17 CFR 201.411(b)(2). This provision instructs the Commission to consider whether the petition for review makes a reasonable showing that (i) a prejudicial error was committed in

[6] BOX had actual notice of the action on March 6, 2015, and BOX filed an Intent Notice on March 13, 2015. See Letter from BOX to Brent Fields, Secretary, SEC, dated March 13, 2015.

the conduct of the proceeding or (ii) the decision embodies: (A) a finding or conclusion of material fact that is clearly erroneous; (B) a conclusion of law that is erroneous; or (C) an exercise of discretion of decision of law or policy that is important that the Commission should review.

Significant Policy Concern that Warrants Commission Consideration

The Capital Plan raises significant policy issues and therefore the Commission should set aside the Approval Order and grant this petition. The Capital Plan, as approved by the Approval Order, fundamentally alters how the OCC functions. Specifically, the Capital Plan changes the nature of the OCC from a non-profit industry utility, operating for the benefit of the options industry, into a for-profit monopoly operating for the benefit of its exclusive group of Shareholder Exchanges. As mentioned above, the OCC is solely responsible for clearing all listed options transactions and is not subject to competitive pressures when setting fees due to its unique status as a monopoly, unlike option exchanges which face ever increasing competitive pressures when setting fees. The unique structure of the OCC alone raises policy concerns that need to be addressed by the Commission; however, there are at least three additional unique factors inherent in the OCC structure that raise policy issues as well, as explained in more detail below.

The first factor is the fact that there is no over-the-counter market for listed options transactions. This means that every options transaction must be cleared through the OCC and broker-dealers cannot engage in internal compression or netting to reduce their exposure to the OCC's fees. This means further that broker-dealers must pay the OCC's fees regardless of the level at which they are set since no alternative exists.

Second, the OCC is owned by only four exchange operators (*i.e.* CBOE, NYSE, NASDAQ, and ISE). This means that any payment from the OCC to the Shareholder Exchanges will consequently put the non-Shareholder Exchanges, including BOX, at a direct competitive disadvantage. This is especially true in this case, where the Capital Plan provides for large annual dividend payments to the Shareholder Exchanges, which will give them an unfair advantage over the non-Shareholder Exchanges. This advantage will have devastating effects on the competitive balance of the options industry by allowing the Shareholder Exchanges to use the dividend payment to subsidize operation costs, which in turn would force the non-Shareholder Exchanges to reduce trading fees to unsustainable levels in an attempt to simply remain competitive with the Shareholder Exchanges.

Third, each of the four Shareholder Exchanges possesses a veto right over certain OCC affairs, including the issuance of new equity that could dilute its ownership.[7] This calls into question whether any changes to the OCC's capital structure is fair and reasonable since any one Shareholder Exchange could veto the changes and hold out for greater benefits, including a higher rate of return on its capital. In theory, even if the Board received an offer on better terms, the offer could be rejected by any of the Shareholder Exchanges if it had the effect of diluting its ownership stake. Any such veto would require the Board to accept terms from the Shareholder Exchanges that may be less favorable to the OCC, the non-Shareholder Exchanges, options investors, and the public.

These unique factors inherent in the OCC structure raise policy issues that need to be addressed by the Commission. As approved, the Capital Plan will allow the OCC to funnel

[7] BOX understands that private shareholder agreements between each of the four Shareholder Exchanges and the OCC include a provision requiring unanimity of the Shareholder Exchanges in order for the OCC to take certain actions, including, at minimum, actions that would have the effect of diluting each of those shareholder's equity stake in the OCC.

wealth to the Shareholder Exchanges while harming the options industry as a whole, including retail customers.

Deficiencies in Staff's Approval of the Filing

In addition to the urgent policy issues mentioned above that require Commission review, the Commission should set aside the Approval Order because many of the Staff's findings are either erroneous or unsupported by any facts or analysis.[8]

A. The OCC Failed to Abide by its own By-Laws

The Staff improperly concluded that the OCC followed the correct governance procedures when debating, approving, and filing the Capital Plan. When, in 2002, the OCC removed the requirement that all national securities exchanges for which the OCC provides clearing services be owners of the OCC, the OCC stated that OCC management "will promptly pass on to non-equity exchanges any information that management considers to be of competitive significance to such exchanges disclosed to exchange directors at or in connection with any meeting or action of the OCC board or any board committee."[9] Also, in order to be fair to the non-Shareholder Exchanges, "the OCC represented to the Commission that OCC management will provide non-equity exchanges with the opportunity to make presentations to the OCC board or appropriate board committee upon request."[10] Additionally, the OCC's By-Laws were amended to include the following provision:

> Non-equity Exchanges will be promptly provided with information that the Executive Chairman considers to be of competitive significance to such Non-Equity Exchanges that was disclosed to Exchange Directors at or in connection

[8] See supra note 4.
[9] See supra note 6 of the 2002 Filing.
[10] Id.

> with any meeting or action of the Board of Directors or any Committee of the Board of Directors.[11]

The OCC failed to provide prompt notice to the non-Shareholder Exchanges in direct violation of the above mentioned provision of the OCC's By-Laws and therefore deprived the non-Shareholder Exchanges of their right to make a presentation regarding the Capital Plan to the OCC Board. This failure by the OCC was brought to the attention of the Staff through comment letters submitted by BOX and BATS explicitly raising this issue.[12] However, the Staff rejected the argument by simply saying that they had no basis to dispute the OCC's position that their Board of Directors conducted the process in conformity with applicable law and the OCC's own By-Laws.[13]

This is troubling for at least two reasons. First, it is hard to understand how the Staff can claim they have no basis to dispute the OCC's position since both BOX and BATS raised issues with the process undertaken by the OCC's Board. The Approval Order does not give an explanation other than that the "OCC confirmed that OCC and its Board of Directors conducted its business in conformity with its By-Laws identified in the comment letters [submitted by BOX and BATS]."[14] However, no formal comment letter was submitted by the OCC addressing the issue of failure to provide prompt notice to the non-Shareholder Exchanges as highlighted by both BOX and BATS. Therefore, it is unclear how the Staff concluded that the OCC satisfied its requirement to provide prompt notice. Two possible explanations exist, both of which fail. The first is that the Staff concluded the Capital Plan was not of "competitive significance" and therefore the OCC was not required to promptly disclose it to the non-Shareholder Exchanges.

---

[11] See Interpretations & Policies .01 to Article VIIB of the OCC's By-Laws.

[12] See Letter from Tony McCormick, Chief Executive Officer, BOX, to Brent Fields, Secretary, SEC, dated March 3, 2015. See also Letter from Eric Swanson, General Counsel and Secretary, BATS Global Markets, Inc., to Brent Fields, Secretary, SEC, dated March 3, 2015.

[13] See Approval Order at 46.

[14] See supra note 113 of the Approval Order.

This view is unsustainable for the many reasons outlined in this petition and specifically due to the competitive issues surrounding the undue burden on and discrimination against the non-Shareholder Exchanges. Second, it could be argued that the Staff concluded that the public notice of the rule filing amounted to prompt notice, thereby satisfying the OCC obligation to promptly notify the non-Shareholder Exchanges of issues of competitive significance, but this justification again falls short. By the OCC's own admission, the process of developing and approving the Capital Plan took nearly a year.[15] Therefore, the Board was well aware of the Capital Plan months before the rule filing was published and had ample opportunity to provide notice to the non-Shareholder Exchanges long prior to the public filing as it should have, and was required to have, done. This justification also contradicts the plain meaning of the word "promptly," which is defined by Webster as "without delay." It is hard to comprehend how the public notice of the Capital Plan amounted to providing notice without delay to the non-Shareholder Exchanges since the OCC had been working on the Capital Plan for nearly a year before it was published.

Additionally, the 2002 Filing represented that the OCC would allow the non-Shareholder Exchanges to make presentations to the OCC's Board.[16] If the public notice of the Capital Plan is considered prompt notice, then the non-Shareholder Exchanges would not have had an adequate opportunity to make a presentation to the OCC's Board on the matter. This contradicts the representations made by the OCC to the SEC in the 2002 Filing and led directly to the current situation in which the non-Shareholder Exchanges have been prevented from making a presentation to the OCC Board. If the OCC had given the required notice to the non-Shareholder Exchanges, preferably months before the Capital Plan was publicly published, then the non-Shareholder exchanges would have had the opportunity to present a competing proposal to the

[15] See Comment Letter from James E. Brown, General Counsel, OCC, dated February 23, 2015, at p. 4.
[16] See supra note 8.

OCC's Board, most likely offering more fair and favorable terms to the OCC. The OCC's failure to provide this opportunity to the non-Shareholder Exchanges directly conflicts with representations made by the OCC and the spirit of the OCC's By-Laws.

Other issues exist with respect to the OCC's approval process that raise significant issues that should be reviewed by the Commission. Most notably is the fact that none of the five directors representing the Shareholder Exchanges recused him/herself from consideration of the Capital Plan. These directors were present for both the deliberations and vote on the Capital Plan even though the Capital Plan represents an obvious conflict of interest due to their financial interest. This seems to conflict with the OCC's Charter and Code of Conduct for OCC Directors. Specifically, Article V of the OCC's Charter states that "[e]ach Director is required to act in good faith in the best interests of the OCC and with due regard to the fiduciary responsibilities owed to OCC as a business and systemically important financial market utility. In addition, each Director is required to comply with the provisions of the Code of Conduct for OCC Directors, including, without limitation, the provisions relating to conflicts of interest and confidentiality."[17] The actual Code of Conduct is not publicly available; however, the OCC does publish its Corporate Governance Principles, which summarize the relevant portions of the Code of Conduct as follows:

> The Board has adopted a Code of Conduct for OCC Directors that includes a Conflict of Interest Policy. The Conflict of Interest Policy incorporates various provisions of applicable corporate law and other standards adopted by OCC to ensure that Board and committee decisions are not impacted by conflicts of interest. Directors are expected to avoid any action, position or interest that conflicts with an interest of OCC, or gives the appearance of a conflict, in accordance with the Conflict of Interest Policy. OCC annually solicits information from directors in order to monitor potential conflicts of

[17] OCC Charter, *available at*: http://www.optionsclearing.com/components/docs/about/corporate-information/board_of_directors_charter.pdf

> interest and directors are expected to be mindful of their fiduciary obligations to OCC as set forth in the Code of Conduct.[18]

It is obvious that each of the directors representing the Shareholder Exchanges had a significant interest in the Capital Plan, yet none of them recused themselves from the deliberations or vote. The Shareholder Exchanges had an interest in receiving the highest possible return for their capital contribution in addition to favorable provisions on their investment to the detriment of the OCC, the non-Shareholder Exchanges and the options industry in general.

The OCC failed to maintain the number of public directors as required by the OCC's By-Laws and, at the time of the OCC Board's approval of the Capital Plan, the Board was missing two public directors.[19] Having these public directors present during the deliberations would have provided valuable input from disinterested directors. Disinterested directors would be most likely to support an outcome that is objectively in the best interest of the OCC and the public, generally, and not a mechanism for funneling wealth to the Shareholder Exchanges. Additionally, there is no indication from the record as to what, if anything, the three public directors who were present did to ensure the Capital Plan was fair and in the best interests of the OCC and the public, generally.

To be clear, BOX is not arguing that every board action which precedes an SRO rule filing must be scrutinized by the Commission prior to Commission action. The reason this particular action should be scrutinized is because of the unique role and structure of the OCC. In addition, from the record it appears that there were significant flaws in the OCC's governance

---

[18] OCC Board of Directors Corporate Governance Principles, *available at* http://optionsclearing.com/components/docs/about/corporate-information/board_corporate_governance_principles.pdf

[19] The OCC's By-Laws require five (5) public directors. See Article III of the OCC's By-Laws.

process. It does not appear that the Staff adequately looked into these concerns and, for that reason, the Commission should examine the governance process of the OCC.

B. Burden on Competition

The Staff improperly concluded that the Capital Plan is consistent with Section 17A(b)(3)(I) of the Act,[20] which requires that the rules of a registered clearing agency do not impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act. The Staff acknowledges that "a dividend that does not accurately reflect the true risk of the investment may result in a burden on competition on one group versus another."[21] The Staff further reasoned that the level of the burden on competition depends on whether the dividend payment is high or low relative to the true cost of capital.[22] However, the Staff incorrectly concluded that since the OCC is not publicly traded, the "OCC's Board of Directors must use its judgment to determine the appropriate or competitive rate of return and the dividend policy that appropriately reflects the risk of the Exchanges' equity investment."[23] This is simply untrue; companies that are not publicly traded routinely raise capital through competitive processes that are not left solely to the judgment of the board of directors. Due to the concerning fact, as mentioned above, that the directors representing the Shareholder Exchanges were present for the deliberation and voting of the Capital Plan, a competitive bidding process would have been extremely beneficial for the OCC's Board. A competitive bidding process would serve to validate that the Board was fulfilling its fiduciary obligations. For these reasons, the Staff

[20] 15 U.S.C. 78q-1(b)(3)(I).
[21] See Approval order at 44.
[22] See Approval order at 45.
[23] Id.

incorrectly concluded that the only way of determining an appropriate rate of return was a subjective one left solely to the Board's judgment.[24]

Another disturbing conclusion reached by the Staff is the fact that, although the Staff recognized that the Capital Plan may result in some burden on competition, the Staff rejected the idea that the burden was undue. Specifically, the Staff found that "such a burden is necessary and appropriate in furtherance of the purposes of the Act given the importance of OCC's ongoing operations to the U.S. options market and the role of the Capital Plan in assuring its ability to facilitate the clearance and settlement of securities transactions in a wide range of market conditions."[25] This reasoning completely avoids the key issue of whether the Capital Plan is the best of all available alternatives for capitalizing a regulatory monopoly. This conclusion reached by the Staff is contrary to the facts on this matter. It appears that the Staff is stating that the burden is not undue because capitalization is necessary and appropriate in furtherance of the Act, regardless of the terms. Due to the unique factors of the OCC and its monopoly position, the Staff should have determined whether the structure of the proposal and the amount of the subsidy that will be paid to the Shareholder Exchanges constitutes an undue burden on competition. Section 3(f) of the Exchange act provides that:

> [w]henever … the Commission is engaged in … the review of a rule of a self-regulatory organization, and is required to consider or determine whether an action is necessary or appropriate in the public interest, the Commission shall also consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation.[26]

Section 3(f) of the Exchange Act requires an examination of the economic effects of a proposed rule and prohibits the Commission from imposing undue burdens on competition. The Staff

[24] See *Chamber of Commerce*, 412 F.3d at 362 (Commission had an obligation to consider reasonable suggested alternatives to conditions imposed by rule).
[25] See Approval order at 45.
[26] See 15 U.S.C. 78c(f).

failed to fully justify how the Capital Plan would not impose an undue burden on competition. Further, the Staff's finding that the level of dividend is irrelevant since the Capital Plan is appropriate and necessary, constitutes a misunderstanding of relevant issues an erroneous conclusion of law.

The Capital Plan unfairly discriminates against the non-Shareholder Exchanges. As mentioned above, the Capital Plan will directly benefit the Shareholder Exchanges through a dividend stream lasting in perpetuity. Although the exact rate of return has not been publicly disclosed by the OCC, from the information that has been provided it appears that the dividend rate could be almost 20%. This dividend will allow the Shareholder Exchanges to subsidize their trading costs, thereby giving them an unfair competitive edge over the non-Shareholder Exchanges. Historically, the Shareholder Exchanges and non-Shareholder Exchanges have, for the most part, been treated the same by the OCC since both categories are "participants" of the OCC and the OCC acted in the best interest of clearing members and the industry as a whole. Until now, the major difference in the treatment of the two categories was the fact that each Shareholder Exchange is allowed to appoint one director to the OCC's Board. This differential treatment was reasonable due to the fact that the OCC guaranteed certain protections to the non-Shareholder Exchanges, such as allowing them to make presentations to the OCC's Board and promptly notifying them of information that is of competitive significance, and by the requirement of public directors[27] although, as mentioned above, the OCC did not provide these rights to the non-Shareholder Exchanges during the deliberation and approval process of the Capital Plan. Now, with the approval of the Capital Plan, the OCC will unfairly discriminate against the non-Shareholder Exchanges by providing excessive dividends to the Shareholder

[27] See supra note 6 of the 2002 Filing.

Exchanges. These excessive dividends are virtually guaranteed and should be considered more of a subsidy paid to the Shareholder Exchanges. It is clear that this Capital Plan will result in unfair discrimination, and the Staff's failure to find as much constitutes an erroneous conclusion of law.

Another unclear issue is that of the liquidation preference of the new Class C common stock that is being issued as part of the Capital Plan. The OCC represented to the SEC in a comment letter that the Class C common stock would be subordinated to claims of creditors of the OCC.[28] However, the OCC has made previous statements that the repurchase rights of Class A and B common stock ranks *pari passu* with OCC's obligation to repurchase notes from the non-Shareholder Exchanges. [29] Since the new Class C common stock has the same liquidation preference as the Class A and B, does this in turn mean that the Class C common stock is not subordinated to the claims of all creditors? It is unclear from the Approval Order whether the Staff concluded that repurchase rights are different from liquidation preference. BOX believes that further explanation is warranted on this issue.

Conclusion

Given the importance of this proposal and the potentially detrimental impact of the Capital Plan on the U.S. options markets, we believe it is critical that the full Commission evaluate whether it is consistent with the requirements of the Exchange Act. The approval of the Capital Plan will radically alter the options industry by converting the OCC from a non-profit industry utility into a profit maximizing monopoly for the benefit of only four exchanges. This transformation will devastate the competitive balance in the options markets by giving the Shareholder Exchanges an unfair advantage over the non-Shareholder Exchanges; an advantage

[28] See Letter from James E. Brown, General Counsel, OCC, dated February 23, 2015, at 14.
[29] See 2002 Filing at 49730.

that the non-Shareholder Exchanges cannot overcome since they are essentially barred from becoming owners of the OCC.

For the reasons stated in this petition, BOX respectfully requests that the Commission exercise its discretion to review this petition and set aside the Approval Order.

DATED: March 20, 2015

Respectfully Submitted,

Lisa J. Fall
President
BOX Options Exchange LLC
101 Arch Street, Suite 610
Boston, MA 02110