



April 27, 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-2019-19

Dear Ms. Countryman:

BOX Exchange LLC (the “Exchange” or “BOX”) appreciates the opportunity to respond 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

At SIFMA’s request, 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. Each time, the Exchange made clear it would remain available to answer questions and consider ways to amend the Proposal if there were material concerns. SIFMA representatives indicated they would notify the Exchange of any questions or concerns. Because there was no further communication from SIFMA, the SIFMA Letter is surprising, and it comes nearly a month after the expiration of the comment period regarding Amendment No. 2 to the Proposal. It is also disappointing that SIFMA chose to not fully acknowledge these meetings as it presented an incomplete record to the Commission. Nevertheless, the Exchange is pleased to address the SIFMA Letter and believes that its key points are already addressed by the Proposal. Furthermore, the Exchange respectfully submits that the Proposal does not raise novel or wide-reaching issues for equity market infrastructure. It would allow security tokens to be issued, traded, cleared and settled

¹ 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-2019-19 (Apr. 22, 2020) (“SIFMA Letter”).

² Securities Exchange Act Release No. 87287 (Oct. 11, 2019), 84 FR 56022 (Oct. 18, 2020). On January 16, 2020, the Commission published notice of the filing of Amendment No. 1 to the Proposal and instituted proceedings to determine whether to approve or disapprove the proposed rule change. Securities Exchange Act Release No. 88002 (Jan. 16, 2020), 85 FR 4040 (Jan. 23, 2020). The Exchange submitted Amendment No. 2 to the Proposal on February 19, 2020 to amend and supersede the original filing, as modified by Amendment No. 1, in its entirety (“Amendment No. 2”). Securities Exchange Act Release No. 88300 (Feb. 28, 2020), 85 FR 13242 (Mar. 6, 2020). See Letter from Lisa J. Fall, President, BOX Exchange LLC, to Vanessa Countryman, Secretary, Commission, re: File No. SR-BOX-2019-19 (Feb. 19, 2020). The Exchange also submitted a detailed response letter to commenters on April 9, 2020. See Letter from Lisa J. Fall, President, BOX Exchange LLC, to Vanessa Countryman, Secretary, Commission, re: File No. SR-BOX-2019-19 (April 9, 2020) (“April Response Letter”).



just like other equity securities are today, and it includes only a narrowly-tailored blockchain component that would apply to firms that choose to become BSTX Participants.

SIFMA first raises concerns related to the proposed T+1 settlement timing, stating that a “T+1 settlement cycle is incompatible with Regulation NMS,” and that the “entire equity market infrastructure is built and based on this standard settlement cycle of T+2.”³ This is simply not true. As stated in the Proposal, National Securities Clearing Corporation (“NSCC”) already settles equities transactions on a T+1 and T+0 basis in addition to T+2.⁴ For example, the Exchange understands that during the final two months of 2019, NSCC cleared 19,000 transactions on a T+1 basis and 2,000 transactions on a T+0 basis.⁵ Additionally, Rule 15c6-1 under the Exchange Act prohibits a broker-dealer from entering a securities transaction in which settlement occurs “*later than* the second business day after the date of contract” unless the parties expressly agree otherwise at the time of the transaction,⁶ and thus the Proposal, which generally requires T+1 settlement, is consistent with Rule 15c6-1 under the Exchange Act. Similarly, SIFMA notes Rule 611 of Regulation NMS contemplates an exception to the trade through rule for securities transactions that are not “regular way”⁷; however, the exception implicitly recognizes that non-regular way transactions occur within the Regulation NMS regulatory framework.⁸ Thus, both of these Exchange Act rules expressly contemplate that transactions in equities, including NMS stock, may settle otherwise than on T+2.⁹ Moreover, the ability to settle equity transactions that occur on a national securities exchange on a T+1 basis in fact predates Regulation NMS.¹⁰ For all of these reasons, the Exchange does not believe it is accurate for SIFMA to state that the “entire equity market infrastructure is built and based on [the] standard settlement cycle of T+2.”¹¹ This type of

³ SIFMA letter at 2.

⁴ Proposal at 13246. NSCC has had this functionality even prior to the 2017 shift from T+3 to T+2 settlement. *See e.g.*, Mike Scotti, DTCC Discusses Accelerated Settlement at SIFMA Ops, DTCC Connection (May 18, 2017), available at: <https://www.dtcc.com/dtcc-connection/articles/2017/may/18/dtcc-discusses-accelerated-settlement-at-sifma-ops> (“[I]t is perhaps not as widely known that DTCC clients already have the ability to settle on Trade Date plus one day (T+1) or even same day (T+0).”).

⁵ Proposal at 13246.

⁶ 17 CFR 240.15c6-1 (emphasis added).

⁷ *See* Exchange Act Release No. 51808 (June 9, 2005), 70 FR 37495, n.326 (June 29, 2005) (“Reg NMS Adopting Release”) (noting that “regular way” exception applies to “a transaction that was executed other than pursuant to standardized terms and conditions, for instance a transaction that has extended settlement terms”). The Exchange notes that this statement from the Commission and other parts of the Reg NMS Adopting Release do not reference transactions on shorter settlement terms, and the Exchange understands that Reg NMS rules that implicate the concept of “regular way” primarily relate to execution issues, as opposed to whether a transaction settles on a T+1 versus a T+2 basis. *See also* Reg NMS Adopting Release at n. 831 (providing examples of non-regular way trades relevant to certain rules of Reg NMS, which do not mention shorter settlement terms, and instead list “trades reported after normal trading hours, bunched trades, next-day trades, previous reference price trades, and late trades”).

⁸ 17 CFR 242.611(b)(2).

⁹ Exchange Act Release No. 80295 (Mar. 22, 2017), 82 FR 15564 (March 29, 2017).

¹⁰ *See e.g.*, Exchange Act Release No. 49685 (May 11, 2004), 69 FR 27964 (May 17, 2004) (SR-NSCC-2004-02) (approving a proposal by NSCC to accept non-standard settlement input, including “next day” transactions, under certain conditions and noting that “NSCC provides the same service for New York Stock Exchange (‘NYSE’) and American Stock Exchange (‘Amex’) equity securities . . .”).

¹¹ SIFMA letter at 2.



over generalized and meritless statement is reminiscent of times past when some market participants have lobbied against change – such as during the move in the U.S. markets to decimalization. However, if SIFMA can articulate actual and specific costs and complexities associated with the T+1 settlement timing in the Proposal, the Exchange would welcome that information. To date, no commenter, including SIFMA, has done so.

SIFMA asserts that the Proposal does not detail “the infrastructure needed to manage the security tokens’ distributed ledger technology, including whitelisted wallets and associated recordkeeping.”¹² Market participants that choose not to be BSTX Participants would be under no obligation whatsoever to adopt any infrastructure related to security tokens. 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 token 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.¹³

SIFMA’s characterization of the Proposal as “nothing more than a way to force industry participants to sign up for the Exchange’s blockchain service, adding cost while providing no apparent value to firms, institutional clients, or retail investors” is a gross mischaracterization. The Exchange notes that it is not proposing any fee associated with the ancillary recordkeeping process. Additionally, the end-of-day security token balance reporting process would apply only to firms that choose to become BSTX Participants and would impose only a minimal reporting burden on them similar to other reporting obligations currently required by self-regulatory organizations like large options position reporting.¹⁴ SIFMA similarly mischaracterizes the Proposal as “encouraging the adoption of [distributed ledger technology] with the likely eventual goal of having it become a system for tracking equity security ownership outside of the current system maintained by DTC and broker-dealers.”¹⁵ This statement is unfounded and without merit. The Proposal is bounded by its terms and is designed to operate entirely within the existing equity market structure – including its requirements for clearance through NSCC and settlement through The Depository Trust Company.¹⁶ Any future changes would be subject to the Commission’s rule filing process under Section 19 of the Exchange Act and public notice and comment.¹⁷

Ancillary Recordkeeping

SIFMA asks if “the distributed ledger technology [is] exclusive to BSTX” and what the implications are for having end-of-day position balances publicly available.¹⁸ The distributed ledger technology that would be used is the Ethereum blockchain. It is not exclusive to BSTX. As described in detail in the Proposal, it is an open source public blockchain that supports smart

¹² SIFMA Letter at 3.

¹³ BSTX Participants, however, should likely include in their policies and procedures a process for complying with the end-of-day reporting requirement to promote compliance with proposed Rule 17020.

¹⁴ See e.g., FINRA Rule 2360(b)(5) and Cboe Rule 8.43.

¹⁵ SIFMA Letter at 3.

¹⁶ See Proposal at 13244-46.

¹⁷ 15 U.S.C. 78s.

¹⁸ SIFMA Letter at 5.



contract functionality.¹⁹ To facilitate the ancillary recordkeeping process, issuers of security tokens would be required to establish a smart contract compatible with the BSTX Security Token Protocol, which is publicly available.²⁰ Thus, all market participants would have open access to the distributed ledger technology associated with the Proposal.²¹ As described in the Proposal, the implications of having end-of-day position balances published as ancillary records are that market participants would be able to observe: (i) anonymous wallet addresses assigned to a particular security token,²² and (ii) changes to the end-of-day position balances associated with those wallet addresses over time.

SIFMA also asks whether the ancillary recordkeeping process could be gamed such as by a firm “publish[ing] to the chain that it has a large holding when in reality it does not.”²³ Knowingly reporting a false number of security tokens to the Exchange would be a direct violation of proposed Rule 17020, violate just and equitable principles of trade, and would be subject to disciplinary action by the Exchange. Nevertheless, if a BSTX Participant did try to “game” the ancillary recordkeeping process by, as SIFMA suggests, over- or under-reporting a quantity, it would not have any impact on the ability of the security tokens to trade.

Fungibility

SIFMA asks why security tokens listed on BSTX would not be fungible with another class of securities from the same issuer and what the implications of this might be. Security tokens would not be fungible with another class of securities of the same issuer because no class of an issuer’s securities is fungible with a separate class of its securities – otherwise they would be the same class of security.²⁴ The Proposal does not propose any change to existing framework for different classes of securities and therefore there are no implications stemming from this aspect of the Proposal.

Whitelisted Wallet Address

SIFMA asks how a whitelisted wallet address is obtained, how permissioning is determined, who controls the wallet address, and how whitelisted addresses are maintained during the lifecycle

¹⁹ Proposal at 13246-47.

²⁰ Additional detail on the BSTX Security Token Protocol can be seen in Exhibit 3N to the Proposal, posted on the Exchange’s website starting on page 333 available at: https://lynxstorageaccount.blob.core.windows.net/boxvr/SE_resources/SR-BOX-2019-19_Amendment_2.pdf. The Exchange notes that smart contracts that determine the functioning of Ethereum-based applications can be publicly viewed and are immutable.

²¹ Market participants would not have the ability to modify the underlying source.

²² However, notably, and as detailed in the Proposal, observers of the Ethereum blockchain would not know which wallet address is associated with a given market participant, whether those security tokens are held by the BSTX Participant on a proprietary basis, on behalf of customers or by a carrying firm reporting on behalf of multiple BSTX Participants, or whether the long position balance includes borrowed security tokens. Proposal at 13252. Thus, the Exchange does not believe the information could be used to gain a trading or other advantage over competitors.

²³ SIFMA Letter at 5.

²⁴ For example, Alphabet (Google) has at least two classes of shares—GOOG and GOOGL—each of which have different ticker symbols, different rights associated with each other (e.g., GOOG has no voting rights while GOOGL has voting rights), and different dividend rates and are consequently not fungible with each other.



of the security token and participant accounts. BSTX Participants would obtain a whitelisted wallet address by contacting the Exchange as described in detail in Part II.G of the Proposal.²⁵ As the only source for obtaining wallet addresses, the Exchange would be responsible for permissioning wallet addresses as well.²⁶ Each wallet address is an alphanumeric string of characters assigned to a particular BSTX Participant for the purposes of ancillary recordkeeping. Under the Proposal, a BSTX Participant would not have the ability to move security tokens to or from its wallet address or otherwise “control” the wallet address. The process of reallocating security token balances among different wallet address is a function performed by the Exchange through its relationship with a Wallet Manager(s). Thus, the proposed use of blockchain technology under the Proposal is almost entirely passive for BSTX Participants, but for initially obtaining a wallet address and the end-of-day reporting of balances. Regarding maintenance of whitelisting for the entire life-cycle, the Exchange would be responsible for this function. An unlimited number of addresses may be established for a security token and could be removed as necessary.

Unlisted Trading Privileges

SIFMA asks if other exchanges are in a position to extend unlisted trading privileges (“UTP”) to trade security tokens and what they would have to do to be able to do so. As described in Part II.K of the Proposal and addressed repeatedly in the April Response Letter, any exchange would be free to extend UTP to security tokens consistent with applicable regulatory requirements.²⁷ Security tokens are fully capable of trading on other exchanges or over-the-counter without any ancillary recordkeeping mechanism.

* * *

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 should therefore be approved.

Pease 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'.

Lisa J. Fall
President
BOX Exchange LLC

²⁵ Proposal at 13248.

²⁶ The Exchange is subject to Section 6(b)(2) of the Exchange Act, which generally requires that any registered broker-dealer may become a member of the Exchange. 15 U.S.C. 78f(b)(2). Because the Exchange would also require BSTX Participants to obtain a whitelisted wallet address to trade on BSTX, any registered broker-dealer would be able to obtain a whitelisted wallet address.

²⁷ Proposal at 13253; April Response Letter, *supra* note 2, at 3-4, 7, 9-10, and 16.