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## **Using this study guide.**

This study guide is intended for use prior to attempting the accompanying exam. Read the complete study guide at your convenience before beginning the exam. You may cover the material in one session or break the material into several shorter sessions, whichever best fits your learning style. All answers to exam questions are covered in this document.

Before you begin, you may find it useful to click the thumbnails button to utilize thumbnails for navigating your way through this document. Thumbnails break the document into separate pages. Clicking the third thumbnail quickly advances the screen to the third page, clicking the sixth thumbnail quickly advances the screen to the sixth page, clicking the first thumbnail sends the screen back to page one, etc. Bookmarks operate similarly by advancing to different sections of the document. Simply use your mouse to click on the section of your choice.

## Options II

### Synthetic Options Positions

A long stock position with a long put creates a long call; a short stock position with a long call creates a long put. A long stock position with a short call creates a short put; a short stock position with a short put creates a short call.

If an investor wants to protect a stock position, he may buy an option to hedge his stock position. A put option is used to protect a long stock position and a call option is used to protect a short stock position. If an investor wants to generate income, he may likewise buy an option to do so. A call option is used to generate income for a long stock position and a put option is used to generate income for a short stock position.

### Synthetic Stock Positions

Investors can use options to create synthetic stock positions. A long call and a short put create a long stock position. A long put and a short call create a short stock position.

Because options have high leverage potential, the SROs have set limits for the maximum positions that may be taken. These limits are specific to the underlying security. The three different limits are 4,500; 7,500 and 10,500 depending on how active the underlying stock is. The position limits refer to “up bet” and “down bet.” To decide if an investor is in violation of the maximum limit, the long calls and short puts or the long puts and short calls are combined. Long calls plus short puts equals same side (up) and long puts plus short calls equals same side (down).

Limitations have also been placed on the number of options of the same class (same type and same underlying security) that may be exercised during any five consecutive business days.

“Acting in concert” restrictions are violations of either positions or exercise limits when the trading in more than one account (with a common decision maker) exceeds either or both of the before mentioned limitations. This also applies to registered representatives trading for discretionary accounts.

## Debt Options

Calls and puts for U.S. Treasury securities work in a similar way to calls and puts for stocks. Two kinds of debt options have been approved for trading. Price-based options give the owner the right to call or put a specified underlying debt security. Yield-based options are cash-settled based on the difference between the exercise price and the value of the underlying yield.

If an investor expects a bond or note price to increase, he could buy a call option with the right to buy the bond or note at a fixed price. If he expects the value of the bond or note to decrease, he could buy puts to sell the bonds or notes at a fixed price. If the investor expects yields to increase, he could purchase a yield-based option for a call and if he expects yields to decrease, he could buy a yield-based option for a put. If an investor buys a price-based option for a call of a T-bond, he is actually expecting a downturn in interest rates. Purchase of a priced-based option for a put of a T-bond shows that the investor is expecting a rise in interest rates. It is important to think of changing interest rates, not prices, as affecting the value of debt options. When interest rates go up, bond prices go down. When interest rates go down, bond prices go up. Yield-based calls increase in value as yields rise; puts increase in value as yields decline.

All yield-based options may only be exercised on the business day prior to expiration. With equity options and price-based options, an underlying security is used, but for yield-based options, the “underlying yield” is used. This is the annualized yield to maturity of the most recently issued treasury security of the specifically designated maturity used for that option. The underlying yield changes every time a new 30-year Treasury Bond is auctioned. During the life of a particular option, the underlying yield may change several times. The yield to maturity is stated in terms of a yield indicator or the maturity percentage multiplied by 10. If the most recent 30-year Treasury bill had a yield to maturity of 6.75%, the yield indicator would be 67.50.

## Foreign Currency Options

A foreign currency option is the right to buy or sell a stated number of units of the underlying foreign currency at a specific price per unit (of U.S. dollars) during a given period of time. It is important to think in terms of

currency exchange rates and dollar strength or weakness. If an investor expects a currency to decrease in value compared to the U.S. dollar, he may try to profit by buying put options. He would anticipate selling at a higher price than market price by the time the option expires.

Investors want to be able to buy the foreign currency below its current market value or sell the currency above its current market value in order to realize profits. A foreign currency call option gives the holder the right to buy foreign currency and a foreign currency put option gives the holder the right to sell foreign currency. There are no options on U.S. dollars.

## Index Options

If an investor expects an upturn in the market as a whole, but doesn't want to wager on only one security, he may use an index that measures the market performance of a broad range of companies and industries as a whole. The index will increase if the market value of the underlying stocks increase and decrease if the market value of the underlying stocks decrease. An investor may purchase index options to profit from anticipated changes in an index.

An index call option will be in-the-money if the index is higher than the strike price and an index put option is in-the-money if the index is lower than the strike price. When an index option is exercised, no stock is delivered. The exercise of a call or put index option gives the holder the in-the-money cash difference between the closing price of the underlying index and the strike price of the option, multiplied by a specific index multiplier (normally \$100). If Ms. Jones bought a New York Stock Exchange Composite Index (NYA) April 260 Call for 3, and the NYA is now 267.5, the option is in-the-money by 7.5 points. If Ms. Jones exercises her option, she will receive a "cash settlement" of  $7.5 \times 100$  or \$750. The call writer to whom the option was assigned must pay Ms. Jones \$750.

Mr. White bought a Standard & Poor's 100 Index (OEX) July 460 Put for a premium of  $4\frac{3}{4}$  and the Index fell to 4.53. If Mr. White exercises the put option, he will get a cash settlement from the writer for \$700 (7 points in-the-money  $\times 100$ ).

## Capped Index Options

Capped Index Options are options on the S & P 100 Index (OEX CAPS) and the S & P 500 (SPX CAPS). These options have most of the same features as standard index options with some features specific only to them. Premiums are quoted in fractions and multiplied by 100 just as other index options and stock options. The strike or exercise price intervals are 30 points. The contracts expire on Saturday following the third Friday of the expiration month, just like other stock and index options. The settlement is by cash payments.

CAPS listings show the “at-the-money” strike price and a capped price that is 30 points in-the-money. This leaves a limited range of participation. If the S & P 100 index is now at 330, calls with a strike price of 330 would be introduced which have a maximum capped price of 360 and puts would have a strike price of 330 and a maximum downside price of 300. Because the profit potential is limited to the difference between the strike price and the capped price, the premiums are normally cheaper than standard index options. The writer of the options doesn’t have the unlimited loss potential either.

These options are automatically exercised if the index price reaches the capped price. If this occurs, the settlement is two business days after tender of the exercise notice to the OCC. If Ms. Green bought one OEX CAPS 300 put for a premium of  $2\frac{1}{4}$  when the index is at 290, the maximum potential loss is \$225 because the most an investor can lose on a long option is the premium paid. The maximum potential gain is \$2,775 because the index could fall to 260, the option would be automatically exercised and Ms. Green would receive the capped price of \$3,000 ( $290 - 260 = 30 \times 100 = 3,000$ ). \$3,000 less the premium of \$225 would yield a profit of \$2,775.

If the capped price is never reached and an option is never automatically exercised during the life of the contract, the option may be exercised on the final day before the expiration. If this happens, the settlement is on the next business day with the owner getting the intrinsic value just as with all other index options.

The basic option strategies are the same as otherwise. For protection, an investor should buy calls in a bull market and buy puts in a bear market. For income or partial protection, an investor should sell puts in a bull market and sell calls in a bear market.

### **Long-Term Equity Anticipation Securities (LEAPS)**

The usual lifetime of options for equities or an index is months and does not match the usual lifetime for stocks which is decades. Because of this mismatch, LEAPS came into being. LEAPS are the first long-term options on individual stocks and the S & P 100 and 500 indexes. The features of LEAPS are by and large the same as those of other stock options, but the expiration date is longer, usually up to 3 years. All equity LEAPS may be exercised anytime before expiration. All index LEAPS may be exercised only at expiration.

Liquidity of LEAPS should be a consideration. Time value for these options is a big factor in the premium because the expiration is longer than usual.

### **Options Margins**

As specified in Regulation T, options are not marginable securities. That is, any investor who wants to buy a put or a call option must pay the premium in its entirety. With Regulation T at 50%, Ms. Finn bought 100 shares of XYZ at \$45 per share and one XYZ Feb 45 put for a premium of 3. Her required margin is  $\$45 \times 100 (\$4500) \times .50 (50\%) = \$2250$  plus \$300 for the put option for a total of \$2550.

When an investor writes both puts and calls (uncovered or naked) options, margin calculations are used. Margin requirements for writers of uncovered options give the broker/dealer protection if the client doesn't live up to his financial obligations. The firm can use the money set aside as the margin requirement to meet the obligation without having to bear the financial loss itself.

## Options Trading

### Newspaper Listings

Newspaper listings show the closing prices for the previous day's trading. The listing includes the underlying security the option holder can buy or sell, the closing price of the stock, the available strike prices, the available expiration months and the closing prices or premiums on the particular option. An "r" in the premium column indicates that the option did not trade on the previous day and an "s" means there is no series of options available. A price spread is referred to as a vertical spread and the strike prices are presented vertically. A time or calendar spread is called a horizontal spread and the months are presented horizontally.

The largest exchange for listed options trading is the Chicago Board Options Exchange (CBOE). Listed options are securities that are bought and sold through brokers in a similar way as stocks. Sales are recorded just as stocks would be. There is a secondary market where holders of long positions can close them by selling the options to other investors. Option writers with short positions can close their positions by buying an option with the same terms as the option just sold, thereby terminating their obligation.

The Options Clearing Corporation (OCC) is owned by the exchanges where options are traded and acts as the clearing agency for listed options transactions. All transactions that open or close positions in listed options are recorded on the OCC books in order to maintain a centralized record keeping system. The OCC is considered the issuer of all listed option contracts. The OCC also serves as guarantor of listed options because it imposes financial requirements on its members. This insures that holders of puts and calls are given certain rights and lends credibility to the listed options market place.

Only stocks that have closed over \$10 per share for each day of the last three months have listed options. The OCC sets this as the criteria to be met to insure stability, liquidity, and adequate public interest for viable options contracts. Furthermore, if the stock closes below \$5 per share for the majority of days during a six-month period, the options will be delisted for that stock and no more listed options will be available for that particular security.

## Exchange Markets Operation

Options exchanges are auction markets. The Chicago Board of Options Exchange (CBOE) divides the functions of the floor specialist among several floor workers. The book order is the responsibility of the Order Book Official (OBO) who maintains an orderly market. He accepts only customer market orders and limit orders from floor brokers, is an employee of the CBOE, does no trading for his own account, and executes the trading rotations. Board brokers are approved by the exchange to help the OBO or act in his place in the handling of orders.

Market makers on the CBOE and Registered Options Traders (ROT) on the other exchanges perform a dealer responsibility on the floor, trading for their own account and risk. Once a market maker gives a firm quote on the CBOE, the quote must be honored for 10 contracts.

Floor brokers act as agents and enter orders for their public clients. They are employed by a member firm on all exchanges.

Some of the more active stocks may involve 9, 12 or more series of options trading at the same time. The busiest trading time is almost always at the market opening. Since the OBO/Specialist can't handle all the activity at once, he calls for bids and offers from the trading crowd when the market opens. The opening rotation starts as soon as the underlying security opens in its primary marketplace. It begins with the lowest strike price and nearest expiration month and continues until all the option's series have been opened. A client market order entered before the market opening has priority over all other orders.

The closing rotation occurs on the last business day before the expiration so anyone who wishes to sell may do so. When the market closes, each series closes in rotation from the lowest strike price and nearest expiration to the highest strike and longest expiration month. The OBO/Specialist may use a closing rotation on a very busy trading day to end the extremely heavy volume of trade. The only time a closing rotation is required is on the last day before expiration, but the OBO may use it at other times if he feels it is needed.

If a fast market is declared, the OBO may start an intra-day rotation and enlist the help of other OBOs, board brokers, and clerks to assist in a fair and orderly market and in executing orders. During this rotation no stop, stop-limit,

or Market-If-Touched (MIT) orders may be executed. An intra-day rotation may reopen trading of options if trading has been stopped. If trading on the underlying stock stops, the options normally are stopped also. When the stock begins trading again, the options exchange uses an intra-day rotation to reopen trading on the options for that stock.

## **Client Options Transactions**

Even after a customer's account has been approved for other kinds of securities transactions, the account must be re-evaluated and approved for options transactions. Furthermore, a client's account may be approved only for particular types of options transactions and not for others. Any changes in the approval must be in writing. A client may be approved for discretionary or non-discretionary transactions. Sometimes the member firms may invoke a minimum dollar amount for accounts in certain options or may enforce dollar limitations on those accounts.

Records of all options customers, dates of account approval and signature of the ROP who approved the accounts must be maintained in written form. Within fifteen days after the account is approved for options, the firm must have a written account agreement signed by the client. The agreement must include the customer's approval that the account be handled in compliance with applicable rules of the OCC and the SROs. The client must also agree to abide by the rules of position and exercise limits.

The firm may include, at its discretion, an explanation of the obligations for any client who writes options. In the agreement, the customer may give the firm discretion limited to the closing out of open contracts just before the expiration of the option. The firm may include a stipulation that the customer is agreeing to notify the firm of any major changes that have taken place in the client's investment objectives or financial status. This obligation is, in fact, required for the client account statements.

The agreement should include the client's acknowledgement that he/she has received a current Options Disclosure Document. This insures that the firm has made full and complete disclosure. The need for approval for all public clients is meant to assure that the firm has exercised due diligence to determine that options transactions are appropriate for the client given his/her investment objectives and financial status, and that the customer has been told the risks of

options transactions. This includes an effort to gather certain minimum information about the customer's financial background.

If options are being traded by a third party, the firm must satisfy itself that the agent actually has authority to act on behalf of the customer and that the authority includes options trading. Likewise, before the firm approves accounts of trusts, pension funds, profit sharing plans, or other fiduciaries for options trading, the firm should determine if the fiduciary's responsibility includes options trading.

### **Background Information for Options Customers**

Before an investment firm may approve a customer for options trading, the following information must be requested:

- ◆ Investment objectives.
- ◆ Employment status.
- ◆ Estimated annual income (this must include all sources).
- ◆ Estimated net worth (minus the family residence).
- ◆ Estimated liquid net worth.
- ◆ Marital status and number of dependents.
- ◆ Age.
- ◆ Experience in investments and knowledge of the industry.

If applicable, the customer's account must include:

- ◆ Information regarding the source or sources of all personal data, including the basis of any estimates.
- ◆ A written agreement must be on file if the client has given discretionary trading authority to anyone. The records must include the name, relationship to the client, and the experience of the one who has the discretionary power.
- ◆ The date the ODD was given to the client.
- ◆ The nature and types of transactions allowable for the account and whether the account is discretionary.
- ◆ The name of the registered representative who will handle the account.
- ◆ The name of the ROP who approved the account and the date of approval.
- ◆ The dates of verification of currency of the account information.

In order to insure that all required information is sought, firms should have uniform account information and approval forms. If a customer refuses to give any required information, the form should indicate this. It is the CROP's

responsibility to review a firm's account approval procedures to determine if and to what extent clients should be approved for options trading.

The background and financial information which was used to approve options trading for a new client must be sent to the customer for verification within 15 days after the client has been approved and the client must be given an opportunity to correct or complete the information. The exception to this rule is if the customer submitted the original information directly and in writing. If so, the firm does not have to resubmit the information to the client. If the firm learns of any material change in a client's financial situation, the data on file must be sent to the client for updating within 15 days after the firm learns of said changes. If a client does not inform the firm of any corrections, the firm may assume its current information is accurate.

### **Options Disclosure Document**

The prospectus delivery requirements of the Securities Act of 1933 are fully applicable to the offer and sale of customers of put and call options. Because of SRO rules, the prospectus must be issued to buyers and sellers. A client must be given the current Options Disclosure Document of the SROs, either before or at the time the account is approved for options trading. Anytime the ODD is revised or amended, the client must be given a copy of the new version or any ODD supplement at least by confirmation time of the next options transaction.

Procedures to verify that a firm is in compliance with these rules must be developed. There are three common methods of doing so. The first is that a firm may request each customer to sign, date, and return a receipt for the ODD. Secondly, the firm may include a narrative in the options account agreement which says that the ODD has been provided. Thirdly, the firm may opt to mail all clients the ODD from the firm headquarters. Either of these methods is adequate if it shows that clients are provided with the ODD at or prior to the time the account was approved for options trading. Verification for receipt of subsequent revisions is also needed.

If a firm sponsors community options seminars, it is appropriate to give attendees a copy of the current ODD. To do so is actually a requirement if any written materials are disseminated at the seminar. Such a practice may satisfy prospectus delivery requirements under the 1933 Act and SRO rules. Proof of this type distribution must be maintained by the firm if any class member

subsequently receives approval from the firm to trade in options. The methods a firm uses to comply with the prospectus delivery requirements need to be delineated in the firm's supervisory procedures.

## **Handling Clients' Options Transactions**

Basically the rules of the SROs that deal with suitability require that any person at a member firm who recommends options trading to a customer must have reasonable grounds to believe that the recommended transaction is not unsuitable for the client. No recommendation for an opening transaction in an option contract may be made unless the person making the recommendation has a basis for thinking the client has enough knowledge and experience in financial matters to be reasonably able to evaluate the risks of the recommendation and is financially able to withstand the risks of the recommended options position. Firms often mark order tickets "unsolicited," "solicited," "recommended," or "not recommended" in order to comply with these rules.

The person from the firm who makes these recommendations must use the information obtained in response to the inquiry of the customer relating to his investment objectives and financial situation and other information actually known to determine suitability. The risks involved in the purchase should be considered and, if appropriate, brought to the attention of the client.

There are specific rules to govern all forms of communication with clients relating to options. These include advertisements, sales literature, options strategy worksheets, descriptions of options programs, firm-sponsored options seminar presentations, and all other communications dealing with options available to customers or the public. Such communications must be balanced, truthful and tasteful. All statements must be accurate and there may not be any omission of pertinent facts. Equal emphasis must be given to advantages and disadvantages of options. Said communications must be truthful and not in any way mislead the client.

The firm CROP has the responsibility for approving all advertisements, educational materials, and sales literature given to customers. The SRO must also approve all ads and educational materials, but not sales literature due to the enormous volume involved. Normally the SROP develops these materials, but does not have the main responsibility for approving them.

## **Guidelines for All Written and Oral Options Communications:**

- ◆ Must not have any falsehoods or leave out any material facts.
- ◆ Must not include any promise for specific results or exaggerated, unwarranted, or unreasonable claims, opinions, or forecasts.
- ◆ Must not have illegible, confusing, or ambiguous clauses or disclaimers.
- ◆ Must meet overall standards of tastefulness.
- ◆ Must adhere to the prospectus delivery requirements of the Securities Act of 1933.

## **General Guidelines for Written Options Communications**

- ◆ Must contain a balance of potential profit making statements and reference to risks.
- ◆ Should not imply that options trading is appropriate for all investors.
- ◆ Should make no guarantees concerning the availability of a secondary market for options.

## **Specific Standards for Advertisements**

- ◆ Must be limited to general descriptions of the issue being offered.
- ◆ Must include where the ODD may be obtained.
- ◆ May include a short description of options.
- ◆ May include requirements of any applicable state law or administrative authority.
- ◆ Must not include any misleading designs or devices.
- ◆ Must not include any use of past recommendations or projected future performance figures.

## **Specific Standards for Sales Literature**

If requested, the firm must provide supporting documentation for projected performance figures or past performance data concerning recommendations.

Sales literature may have projections of future performance if:

- ◆ No mention is made of certainty concerning the future performance.
- ◆ All relevant factors are disclosed.

- ◆ The projections are plausible.
- ◆ All material assumptions are so named.
- ◆ All risks are included.
- ◆ The annualized rates of return are not based on less than a 60-day time frame.

Sales literature may include representations of the performance of past recommendations the firm has made if:

- ◆ The material covers only a certain universe and at least the most recent 12-month period.
- ◆ All pertinent costs and all material assumptions used in the annualization process are included.
- ◆ The numbers of recommendations made and the number of advancing vs. declining positions are included in any summary used.
- ◆ General market conditions are disclosed.
- ◆ A ROP concludes that the records are fair and initials the report.
- ◆ The report must declare that the results should not be seen as an indicator of future performance.
- ◆ The client is given the dates and prices of each recommendation, if requested.

Firms may decide whether or not to utilize options worksheets. If used, the worksheets must adhere to all the same requirements as sales literature and a uniform standard must be used throughout the firm.

### **Customer Exercise Notices**

Allocation of exercise notices to customers with short options positions must be fair and non-discriminatory. Allocation must be made either by an approved method of random selection or by using the “first in, first out” method. It is the responsibility of each firm’s CROP that the method of allocation adheres to all the requirements for these options. After the method of allocation is chosen, the firm must notify all its options customers in writing. The method and any consequences to the customers must be identified. Firms must keep sufficient records and work papers to verify precisely how the exercise notice allocation is managed. These records must be maintained for at least three years. The SRO must approve any changes to its plan.

## Manipulation

Unsuccessful and successful manipulation plans may be unlawful. The results of the manipulation are not relevant if the evidence establishes that there was “intent to manipulate.” Capping, supporting, pegging, and frontrunning are illegal forms of manipulation. Capping involves an options trader who is short call options submitting a series of sale orders on stock in an attempt to block the stock price from rising above the strike price of the short calls. If this works, the investor will be able to retain the call options out-of-the-money and prevent the short call options from being exercised. Supporting is the opposite of capping. Supporting involves an options trader who has written puts on a certain security. If the price begins to decrease and the trader believes the puts will be in-the-money, he may buy orders on the underlying stock to try to keep the stock price from declining more. Pegging usually refers to an intention to cause the price of an underlying security to stay at a given price, regardless of whether the price is at, below, or above the strike price of put and/or call options. Pegging essentially encompasses capping and supporting. Pegging may be suspected if an investor buys and/or sells a series of the same underlying stock and it appears he is trying to stabilize its price at a certain level that benefits his total position in that stock. Frontrunning, also referred to as front running of blocks, is when options positions are taken after the firm has received a block order but before the block order is submitted. This benefits the move in the market that the block causes. Frontrunning is not established if the firm executes the client’s order before it enters its options order.

## Options Tax Treatment

The IRS currently regards options held by an investor as capital assets (the same as stocks and bonds). This is true of holders of options, but not writers. If an options holder allows his option to expire unexercised, the full premium is considered a capital loss. The loss is long-term or short-term depending on its holding period. If the holder of an option sells the option in a closing sale transaction before its expiration, the profit or loss is considered a capital gain or capital loss. The amount is computed by comparing the proceeds received and the premium paid for the option. The holding period of the option dictates whether the gain or loss is long-term or short-term. If the investor has multiple options contracts, but does not sell all of them and does not identify which is being closed-out, the IRS assumes FIFO. However, the trader may specify which contract is being closed-out if he prefers. If the investor of a call option exercises the option, the premium he receives is added

to the exercise price to determine his tax basis. He owes no taxes until he sells the underlying stock. The holding period begins when he exercises the stock, not from the date he bought the option. If he kept the stock for more than twelve months after the exercise notice, the gain is long-term. If he sold twelve months or less from the date of the notice, the gain is short-term. If Ms. Finley bought an ABC Nov 30 Call at a premium of 4 and exercised the call, she would have a tax cost basis of \$3,000 plus \$400 or \$3,400. If she sold for \$4,000, she would have a capital gain of \$600. If an investor in a put option exercises it, the premium is subtracted from the exercise price to determine the proceeds.

Gains and losses for put options are always treated as short-term if the security used to exercise the put was bought after the purchase of the put or a substantially identical security has a short-term holding period as of the date of purchase of the put. Gains and losses for puts are considered long-term if the underlying stock used to exercise the put had already been held long-term at the time the put was purchased. Also, if the put and the security used to exercise it were bought on the same day and the put is a “married put,” or a “qualified put,” the holding period of the stock determines whether the put is long or short term. If the married put expires, its premium is added to the cost basis of the long stock position.

The Wash Sale Rules applies to traders who sell a security at a loss and then buy a “substantially identical” security either 30 days before or 30 days after the date of the sale. The IRS will not allow the use of the loss, but washes it away. The wash sale rule applies to a trader who buys a stock, sells it at a loss, and buys a call option on the same security during the wash sale time period. The investor may in fact transact all this, but the loss may not be used. Different options series are not considered identical securities, so an ABC June 35 call sold at a loss with purchase of an ABC Sept 35 call does not violate the Wash Sale Rule.

Options are not considered capital assets for writers. On the contrary, the writer of an asset is said to have incurred a liability for which he is paid a premium. If an option expires unexercised, the premium the writer receives is always considered a short-term gain regardless of how long the investor kept his short position. If an investor writes an option and uses a closing transaction, any profit or loss is considered short-term. If a call writer is exercised, the premium received is added to the exercise price to determine the sale proceeds. If a put writer is exercised, the premium is subtracted from the exercise price to

determine his cost basis and the holding period begins. Some very complicated rules relating to particular deep-in-the-money covered calls exist, but are beyond the scope of this course.



Now that you have completed reading this course, you may proceed to the accompanying exam to earn a verifiable certificate of completion.