# G L O S S A R Y

**ABANDON:** The act of not exercising or selling an option before its expiration.

**ACCRUED INTEREST:** The interest due on a bond since the last interest payment was made, up to, but not including the settlement date. Anyone wishing to buy the bond pays the market price of the bond plus any accrued interest. Conversely, anyone selling a bond will have the proceeds increased by the amount of accrued interest.

**ACQUISITION:** The 'A' in M&A (Mergers and Acquisitions) is when one company buys enough stock of another company to take control of that company. When a take-over attempt is "unfriendly", the buying company may offer a price for the other company's stock that is well above current market value. The management of the company that is being bought might ask for a better stock price or try to join with a third company to counter the take-over attempt.

**ADJUSTED OPTION**: An option resulting after an event such as a stock split (2 for 1 stock split), stock dividend, merger, or spin-off. An adjusted option may represent some amount other than the one hundred shares that is standard in the U.S. For example, after a 2 for 1 stock split, the adjusted option will represent 200 shares. For certain adjusted options, the multiplier of the option may be something other than the $100 that is standard in the U.S.

**AFFIDAVIT OF DOMICILE:** A notarized affidavit executed by the legal representative of an estate reciting the residence of the decedent at the time of death. This document would be required when transferring ownership of a security from a deceased person's name.

**ALL-OR-NONE ORDER (AON):** An order that must be filled completely when the order is executed or not filled at all. In other words, partial fills are not allowed on this type of order.

**AMERICAN DEPOSITORY RECEIPT (ADR):** Foreign company equities traded on a U.S. exchange. The ADR is issued by a U.S. bank in place of the foreign company's shares, which are held in trust by the bank. ADRs facilitate the trading of foreign stocks in U.S. markets. ADRs have exposure to currency fluctuations.

**AMERICAN STOCK EXCHANGE (AMEX):** One of the major stock and option exchanges in the U.S. It is located in the financial district of New York City.

**AMERICAN-STYLE OPTION:** An option contract that can be exercised at any time from the time the option is purchased to the expiration date of the option.

**ARBITRAGE:** The simultaneous purchase and sale of identical or equivalent financial instruments in order to benefit from a discrepancy in their price relationship. More generally, it refers to an opportunity to make risk-free returns that are greater than the risk-free rate of return.

**ASK or OFFER:** The price of a stock or option at which a seller is offering to sell a security, that is, the price that investor may purchase a stock or option.

**ASSIGNED:** To have received notification of an assignment on short options by The Options Clearing Corporation through a broker.

**ASSIGNMENT:** When the seller (writer) of an option receives an exercise notice that obligates him to sell (in the case of a call) or purchase (in the case of a put) the underlying stock at the option's strike price.

**AT-THE-MONEY (ATM):** An option is at-the-money when the price of the stock is at or near the strike price.

**AUTOMATED ORDER ENTRY SYSTEM:** Some exchanges have computerized systems designed to route stock and option orders directly to the trading pit. They are intended to speed the execution of orders. These systems generally have limits on the size of orders. Examples of these systems are: RAES, AUTO EX, and SUPERDOT.

**AUTOMATED EXECUTION SYSTEM (AUTO EX):** The automated order routing system on the American Stock Exchange.

**AUTOMATIC EXERCISE:** The Options Clearing Corporation (OCC) uses this procedure to exercise in-the-money options at expiration. Doing so protects the owner of the option from losing the intrinsic value of the option because of the owner's failure to exercise. Unless instructed not to do so by the owner of the option (through the owner's broker), The Options Clearing Corporation will exercise all expiring equity options that are held in customer accounts if they are in-the-money by 75 cents

(3/4 of a point) or more. The OCC will automatically exercise an option position if it is 75 cents (3/4 of a point) or greater in-the-money at expiration unless the owner of the option instructs otherwise.

**BACK MONTHS:** A rather arbitrary term that refers to the classes of options with the expiration months that are further dated the option class with the nearest expiration month.

**BACKSPREAD:** An option position composed of either all calls or all puts, with long options and short options at two different strike prices. The options are all on the same stock and usually of the same expiration, with more options purchase than sold. A backspread is the sale of an option(s) and the purchase of a greater number of the same type of options that are out-of-the-money with respect to the one(s) purchased. For example, an 80/90 put 1-by-3 backspread is long 3*80 puts and short 1*90 put.

**BANK GUARANTEE LETTER:** The document supplied by a bank certifying that a person has a specific amount of funds on deposit with the bank.

**BASIS:** Generally referring to the futures markets, it is the difference between the cash price of the underlying commodity and the price of a futures contract based on that underlying commodity. Cash price minus futures price equals basis.

**BASIS POINT:** A .01% tick on a 1.00% scale used to describe the yields of interest rates or interest rate products. For example, when the U.S. Fed raises the discount rate 25 basis points, the discount rate goes from 5.00% to 5.25%.

**BASIS RISK:** The risk of the basis between the cash price and the future price widening or narrowing between the time a hedge position is implemented and liquidated.

**BEAR:** A person who believes that the price of a particular security or the market as a whole will go lower.

**BEARISH:** The outlook of a person anticipating lower prices in a particular security or the market as a whole.

**BEAR MARKET:** Any market in which prices are trending lower.

**BEAR SPREAD:** Generally speaking, it is any spread that theoretically profits when the market moves down. Specifically it refers to a vertical spread.

**BETA:** A measure of the return (in percentage terms) on a stock relative to the return (in percentage terms) of an index. For example a stock with a beta of .80 should have a percentage net change equal to 80% of the percentage net change of the index. Therefore if the index is down 2% the stock in question should be down 1.6% (.80x2%).

**BID:** The price of a stock or option at which a buyer is willing to purchase a security; the price at which a customer may sell a security.

**BID/ASK (OFFER) SPREAD:** The difference between the bid and ask prices for a particular stock or option.

**BINOMIAL MODEL:** A mathematical model used to price options. Generally used for American-style options, the model creates a binomial lattice to price an option, based on the stock price, strike price, days until expiration, interest rate, dividends, and the estimated volatility of the stock. One of the main differences from the Black Scholes Model is that it factors in the possibility of early exercise of the options.

**BLACK SCHOLES MODEL:** A mathematical model used to price options. Generally used for European-style options, the model prices options using a probability-weighted sum of stock and a bond. Black-Scholes uses the stock price, strike price, days until expiration, interest rate, dividends, and the estimated volatility of the stock as variables in the model.

**BLOCK or BLOCK TRADE:** A large position or transaction of stock, generally at least 10,000 shares or more.

**BLUE SKY LAWS:** The popular name for laws enacted by various states to protect the public against securities fraud. The term is believed to have been coined by a judge who stated that some brokers were selling everything including the “blue sky” to investors.

**BOND:** A debt instrument or promissory note of a corporation, municipality, or the U.S. Government. A bond represents debt on which the issuer of the debt usually promises to pay the owner of the bond a specific amount of interest for a defined amount of time and to repay the loan on the maturity date. Bonds are distinct from stock (equity), which represents ownership.

 

**BOX SPREAD:** An option position composed of a long call and short put at one strike, and a short call and long put at a different strike. For example, a long 50/60 box spread would be long the 50 call, short the 50 put, short the 60 call and long the 60 put. Considered largely immune to changes in the price of the underlying stock, in most cases, a box spread is an interest rate trade. For all intents and purposes, the buyer of the box is lending money to the options market, and the seller of the box is borrowing money from the options market.

**BREAK-EVEN POINT(S):** The stock price(s) at which an option position generates neither a profit nor a loss. An option position's break-even point(s) are generally calculated for the options' expiration date. Option pricing models can be used to calculate a position's break-even point before the options' expiration date.

**BROKER:** A broker is an individual or firm that charges a fee or commission for executing, either on the floor of an exchange or electronically, buy, sell, or spread orders submitted by a customer or firm.

**BROKER LOAN RATE:** This is the interest rate that banks charge brokerage firms to finance their (the brokerage firms) customers' stock and option positions.

**BROKER-DEALER:** Generally, a broker-dealer is a person or firm who facilitates trades between buyers and sellers and receives a commission or fee for his services. When a broker acts in the capacity of a dealer, he may buy and sell stocks and options for his own account, which can generate profits or losses.

**BULL:** A person who believes that the price of a particular security or the market as a whole will go higher.

**BULLISH:** The outlook of a person anticipating higher prices in a particular security or the market as a whole.

**BULL MARKET:** Any market in which prices are trending higher.

**BULL SPREAD:** Generally speaking, it is any spread that theoretically profits when the market moves up. Specifically it refers to a vertical spread.

**BUTTERFLY SPREAD:** An option position composed of either all calls or all puts (with the exception of an iron butterfly), with long options and short options at three different strikes. The options are all on the same stock and of the same expiration, with the quantity of long options and the quantity of short options netting to zero. The strikes are equidistant from each other. For example, a long 50/60/70 put butterfly is long 1*50 put, short 2*60 puts, and long 1*70 put.

**BUY ON CLOSE:** To buy at the end of a trading session at a price within the closing range.

**BUY ON OPENING:** To buy at the beginning of a trading session at a price within the opening range.

**BUYING POWER:** The amount of money available in an account to buy stocks or options. Buying power is determined by the sum of the cash held in the brokerage account and the loan value of any marginable securities in the account without depositing additional equity.

**BUY-TO-COVER:** A buy order that closes or offsets a short position in stock or options.

**BUY-WRITE:** Synonymous to a covered call or covered write, this is a position of long stock and short a number of calls representing the same amount of shares as the long stock position. This position may be entered into as a spread order with both sides (buying stock and selling calls) being executed simultaneously. For example, a buy-write is buying 500 shares of stock and writing 5*50 strike calls.

**CABINET OR "CAB" TRADE:** An option trade at a "cabinet price", which is equal to one dollar. Generally, cabinet trades only occur at very far out-of-the-money options. Cabinet trades are not always available depending on who you clear.

**CALENDAR SPREAD (TIME SPREAD):** An option position composed of either only calls or only puts, with the purchase or sale of an option with a nearby expiration offset by the purchase or sale of an option with the same strike price, but a more distant expiration. The options are on the same stock and have the same strike price. The quantity of long options and the quantity of short options net to zero. For example, long the AUG/NOV 65 call calendar spread is short 1 August 65 call and long 1 November 65 call.

**CALL OPTION:** A call option gives the buyer of the call the right, but not the obligation, to buy the underlying stock at the option's strike price. The seller of the call is obligated to deliver (sell) the underlying stock at the option's strike price to the buyer of the call when the buyer exercises his right.

**CALLED AWAY:** The term used when the seller of a call option is obligated to deliver the underlying stock to the buyer of the call at the strike price of the call option.

**CALL WRITER:** An investor who receives a premium and takes on, for a specified time period, the obligation to sell the underlying security at a specified price at the call buyer's discretion.

**CANCELED ORDER:** An order to buy or sell stock or options that is canceled before it has been executed. Generally, it is easier to cancel a limit order than a market order. A limit order can be canceled at any time as long as it has not been executed. Market orders can get executed so quickly that it is usually impossible to cancel them.

**CAPITAL GAIN OR CAPITAL LOSS:** Profit or loss generated from transactions in stocks, options, bonds, real estate, or other property.

**CARRY/CARRYING CHARGE:** Interest is charged on any money borrowed to finance a position of stocks or options. The interest cost of financing the position is known as the carry.

**CASH ACCOUNT:** An account in which all positions must be paid for in full. No short positions in stocks or options are allowed in a cash account.

**CASH MARKET:** Generally referred to regarding futures markets, the cash market is where transactions are made in the commodity or instrument underlying the future. For example, there are cash markets in physical commodities such as grains and livestock, metals, and crude oil, financial instruments such as U.S. Treasury Bonds and Eurodollars, as well as foreign currencies such as the Japanese yen and the Canadian dollar. As it relates to futures on stock indices, the cash market is the aggregate market value of the stocks making up the stock index.

**CASH SETTLED OPTION:** An option that delivers a cash amount, as opposed to the underlying stock or futures contracts such as with options on stocks or futures, when exercised. The amount of cash delivered is determined by the difference between the option strike price and the value of the underlying index or security. In the U.S., stock index options like the OEX and SPX are cash settled options.

**CHICAGO BOARD OF TRADE (CBOT):** Founded in 1848 with 82 original members, today the CBOT is the one of the largest futures and options exchanges in the world. It is known for its grain and U.S. Treasury Bond futures. Futures and futures options are traded at the CBOT.

**CHICAGO BOARD OPTIONS EXCHANGE (CBOE):** The Chicago Board Options Exchange is currently (2000) the largest option exchange in the U.S. Formed in 1973, the CBOE pioneered "listed options" with standardized contracts. Equity and index options are traded at the CBOE.

**CHICAGO MERCANTILE EXCHANGE (CME):** Originally formed in 1874 as the Chicago Produce Exchange, where products such as butter, eggs, and poultry were traded, the CME is now one of the biggest futures and options exchanges in the world. The CME trades futures on stock indices, foreign currencies, livestock, and Eurodollars. Futures and futures options are traded at the CME.

**CLASS OF OPTIONS (OPTIONS CLASS):** Options of the same type either all calls or all puts on the same underlying security.

**CLEAR/CLEARING:** The process by which orders are accounted for and matched, and funds transferred.

**CLEARING BROKER-DEALER:** A broker-dealer that clears its own trades as well as those of introducing brokers.

**CLEARING HOUSE:** An agency connected with an exchange through which all stock and option transactions are reconciled, settled, guaranteed, and later either offset or fulfilled through delivery of the stock and through which payments are made. It may be a separate corporation, rather than a division of the exchange itself.

**CLEARING MEMBER:** Clearing members of U.S. exchanges accept responsibility for all trades cleared through them, and share secondary responsibility for the liquidity of the exchanges' clearing operation. Clearing members earn commissions for clearing their customers' trades. Clearing members must meet minimum capital requirements.

**CLOSE (C), THE:** The time at which trading on a stock or option ends for the day. In reference to the O,H,L,C "C" represents the closing price of the session.

 

**CLOSING PRICE:** The price of a stock or option at the last transaction of the day.

**CLOSING PURCHASE:** A transaction in which a person who had initially sold short a stock or option exits or closes his short position by buying back the stock or option.

**CLOSING RANGE:** The range of high and low prices, or bid and ask prices, recorded during the close (the final closing minutes of the trading day).

**CLOSING TRANSACTION:** A transaction in which a person who had initially bought or sold stock, futures or options exits or closes (liquidates) his position by selling his long stock, futures or options or buying back his short stock, futures or options.

**COMBO:** Often another term for synthetic stock, a combo is an option position composed of calls and puts on the same stock, same expiration, and typically the same strike price. The quantity of long options and the quantity of short options nets to zero. Buying a combo is buying synthetic stock; selling a combo is selling synthetic stock. For example, a long 60 combo is long 1*60 call and short 1*60 put. Sometimes, combo is used to describe options at two different strikes, in which case it would not be synthetic stock.

**COMMINGLING:** The combining by a brokerage firm of customer securities with firm securities and pledging them as joint collateral for a bank loan; this practice is prohibited unless authorized by customers.(NASD)

**COMMISSION:** The one time fee charged by a broker to a customer when the customer executes a stock or option trade through the brokerage firm.

**CONDOR SPREAD:** An option position composed of either all calls or all puts (with the exception of an iron condor), with long options and short options at four different strikes. The options are all on the same stock and of the same expiration, with the quantity of long options and the quantity of short options netting to zero. Generally, the strikes are equidistant from each other, but if the strikes are not equidistant, the spread is called a pterodactyl. For example, a long 50/55/60/65 call condor is long 1*50 call, short 1*55 call, short 1*60 call, and long 1*65 call. In a long (short) condor the highest and lowest stikes are both long (short) while the two middle strikes are both short (long).

**CONFIRMATION STATEMENT:** After a stock or options transaction has taken place, the brokerage firm must issue a statement to the customer. The statement contains the name of the underlying stock, the number of shares or options bought or sold and the prices at which the transactions occurred.

**CONSOLIDATED TAPE:** The ticker reporting transactions of NYSE listed stocks that take place on the NYSE or any of the other regional stock exchanges. Similarly, transactions of AMEX listed securities, and certain other securities listed on regional stock exchanges, are reported on a separate tape.

**CONTINGENCY ORDER:** When you place a stock or options order you can choose to place contingencies on that order, meaning that the order will be filled only when a specific event has occurred. For example, a contingency order might be, "Buy 10 XYZ 80 calls at the market if XYZ stock trades above 75".

**CONTRACT:** The basic unit of trading for options. An option, whether it's a put or a call, is an agreement between two parties (the buyer and the seller) to abide by the terms of the option contract as defined by an exchange.

**CONTRACT MONTH:** Generally used to describe the month in which an option contract expires.

**CONTRACT SIZE:** The number of shares of the underlying stock that an options contract would deliver if exercised. Contract sizes for equity options in the U.S. are generally 100 shares, unless the contract size has been adjusted for a split, merger, or spin-off. For example, if you are long 1 XYZ 50 call with a contract size of 100 and you exercise that call, you will get 100 shares of XYZ for a price of $50 per share. If you are long 1 ABC 90 call with a contract size of 250 and you exercise that call, you will get 250 shares of ABC for a price of $90 per share. Most software incorporates the contract size in the calculation of your delta and gamma.

**CONVERSION:** A position of long stock, short a call, and long a put (with the call and put having the same strike price, expiration date, and underlying stock). The short call and long put acts very much like short stock, thus acting as a hedge to the long stock. So, a conversion has a very small delta. A conversion is a way to exploit mispricings in carrying costs.

 

**CORRECTION:** A temporary reversal of direction of the overall trend of a particular stock or the market in general.

**COST BASIS:** The original price paid for a stock or option, plus any commissions or fees. It is used to determine capital gains or losses when the stock or option is sold.

**COVER:** Frequently used to describe the purchase of an option or stock to exit or close an existing short position.

**COVERED WRITE OR COVERED CALL OR PUT/COVERD CALL OR PUT WRITING (SELLING):** An option strategy composed of a short call option and long stock, or a short put option and short stock. For example, selling (writing) 2 XYZ 50 calls while owning 200 shares of XYZ stock is a covered call position.

**COVERED WRITER (SELLER):** Someone who sells or “writes” an option is considered to have a "covered" position when the seller of the option holds a position in the underlying stock that offsets the risk of the short option. For example, a short put option is covered by a short position in the underlying stock, and a short call option is covered by a long position in the underlying stock.

**CREDIT:** An increase in the cash balance of an account resulting from either a deposit or a transaction. As it relates to option orders, a credit is how much the premium collected from selling options exceeds the premium paid for buying options.

**CREDIT BALANCE (CR):** This is the money the broker owes the customer after all commitments have been paid for in full. The money could come after a sale of securities, or simply be cash in the customer’s account.

**CREDIT SPREAD:** Any option spread where you collect a credit when you execute the spread.

**CROSSED MARKET:** A situation that occurs on multiple-listed stock and options, where the highest bid price for a stock or option on one exchange is higher than the lowest ask price for that same stock or option on another exchange.

**CROSSING ORDERS:** The practice of using one customer’s orders to fill a second customer’s order for the same security on the opposite side of the market. For this to occur each order must be first offered on the exchange floor; if there are no takers, the broker may cross the orders usually at a price somewhere in between the existing bid and ask prices.

**CURRENT MARKET VALUE (CMV):** The current worth of the securities in an account. The market value of listed securities is based on the closing prices on the previous business day. Syn. long market value (LMV). (NASD)

**CUSTOMER:** Any person or entity that opens a trading account with a broker-dealer. The customer may be classified in terms of account ownership, payment methods, trading authorization or types of securities traded.

**CUSTOMER AGREEMENT:** The document a customer signs when opening a margin account with a broker-
dealer; this document allows the firm to liquidate a portion or all of the customer's account if the customer fails to meet margin requirements set by the firm or Exchange.
**CUSTOMER STATEMENT:** This document displays a customer's trading activity, positions and account balance. The SEC requires the statement be sent quarterly, however, Many firms' customer statements will be sent daily via email or may be accessed on line at anytime day or night.

**DATE OF RECORD (RECORD DATE):** Date on which you must own shares of a stock to be entitled to the dividend payment on that stock. The day after the record date and until the day the dividend is actually paid, the stock trades ex-dividend.

**DAY ORDER:** A day order is an order that is "good for the day" and is automatically cancelled if it cannot be executed the day it was placed. Compare to good-til-cancelled (GTC) orders.

**DAY TRADE:** A stock or option position that is purchased and sold on the same day.

**DAY TRADING:** Buying and selling the same stock or option position in one day's trading session, thus ending the day with no position.

**DEALER:** A firm or individual engaged in the business of buying or selling securities for its own account.

**DEBIT BALANCE (DR):** In a customer's margin account, that portion of the value of stocks that is covered by credit extended by the broker to the margin customer. In other words, the amount of money a customer owes the brokerage firm. (NASD)

**DEBIT SPREAD:** Any option spread where you pay money for the spread. The debit occurs when the amount of premium paid for the option purchased exceeds the premium received for the option sold.

**DECK:** The stack of stock or option orders that are to be filled by a broker on the floor of an exchange.

**DECLARATION DATE:** The date a company announces the payment date, record date and amount of an upcoming dividend.

**DEFERRED:** Refers to “back month” options or futures.

**DELAYED OPENING:** Exchange officials can postpone the start of trading on a stock beyond the normal opening of a day’s trading session. Reasons for the delay might be an influx of large buy or sell orders, an imbalance of buyers and sellers, or pending important corporate news that requires time to be disseminated.

**DELAYED QUOTES:** Stock or option price quotes that are delayed by the exchanges 15 or 20 minutes from real-time.

**DELIVERY:** When referring to stock options, delivery is the process of delivering stock after an option is exercised. If a trader is long a call, and he exercises that call, the person who is short that call must deliver the underlying stock to the trader who is long the call. If a trader is long a put, and he exercises that put, the trader will deliver the underlying stock to the person who is short that put. Actually, the delivery of the stock takes place through clearing firms under very specific terms and procedures established by the exchange where the option is traded. See assignment and exercise.

**DELTA:** An approximation of the change in the price of an option relative to a change in the price of the underlying stock when all other factors are held constant. For example, if a call has a price of $1.5 and a delta of .33, if the underlying stock moves up $1, the option price would be $1.83 ($1.5 + (.33 x $1.00)). Generated by a mathematical model, delta depends on the stock price, strike price, volatility, interest rates, dividends, and time to expiration. Delta also changes as the underlying stock fluctuates. See gamma.

**DERIVATIVE SECURITY:** A security whose value is derived from the value and characteristics of another security, called the underlying security. Calls and puts are derivative securities on underlying stocks.

**DESIGNATED ORDER TURNAROUND (DOT):** NYSE's automated order entry system.

**DIALGONAL SPREAD: L**ong a call (put) in one month and a short call (put) in another month with different strikes

**DOUBLE DIAGONAL:** Two diagonal spreads, one is in the calls and the other is in the puts. AKA Straddle Strangle Swap or Calendarized Iron Wing Spread. Usually configured as short closer dated straddle or strangle protected by wider strike further dated strangle.

**DISCOUNT RATE:** The rate that the Federal Reserve Bank charges on short term loans it makes to other banks and financial institutions.

**DISCRETIONARY ACCOUNT:** An account in which the customer has given the registered representative authority to enter transactions at the rep's discretion.

**DIVIDEND:** A payment made by a company to its existing shareholders. Dividends are usually cash payments made on a quarterly basis. Dividends can also be in the form of additional shares of stock or property.

**DIVIDEND FREQUENCY:** Indicates how many times per year (quarterly, semi-annually) a particular stock pays a dividend.

**DIVIDEND YIELD:** The annual percentage of return that received from dividend payments on stock. The yield is based on the amount of the dividend divided by the price of the stock and of course fluctuates with the stock price.

**DON'T KNOW (DK) NOTICE:** A term used when brokers or traders compare confirmations on a transaction. If one party receives a confirmation on a trade that it does not recognize, that party would send the other party a D.K. notice.

**DOWN-TICK:** A term used to describe a trade made at a price lower than the preceding trade. A short sale may not be executed on a down or minus tick.(NASD)

 

**DOWNTREND:** Successive downward price movements in a security over time.

**DUAL/MULTIPLE LISTED:** When the same stock or option is listed on two or more different exchanges. For example, IBM options are traded on the CBOE, PHLX and AMEX.

**DUPLICATE CONFIRMATION:** SRO regulations require a duplicate confirmation (of a customer's confirmations) be sent to an employing broker-dealer, if the customer is an employee of another broker dealer. Also, this duplicate confirmation may be sent to a customer's attorney if the request is put in writing. (NASD)

**EARLY EXERCISE:** A feature of American-style options that allows the buyer to exercise a call or put at any time prior to its expiration date.

**EQUITY:** Equity can have several meanings, including 1) stock, as it represents ownership in a corporation, or 2) in a margin account, equity represents a customer's ownership in his account; it is the amount the trader would keep after all his positions have been closed and all margin loans paid off.

**EQUITY OPTIONS:** See Stock options.

**EUROPEAN-STYLE OPTIONS:** An option contract that can only be exercised upon its expiration date. Compare to American-style options.

**EXCESS EQUITY:** The value of cash or securities held in a margin account that exceeds the federal requirement. (NASD)

**EXCHANGE:** An association of persons (members) who participate in buying and selling securities. It also refers to the physical location where the buying and selling takes place.

**EXCHANGE-LISTED SECURITY:** Securities that have met certain requirements and have been admitted for full trading privileges on an exchange such as the NYSE or AMEX. These securities will have a three letter designation (IBM) rather than a four letter designation (MSFT) for over-the-counter securities.

**EX-DIVIDEND:** Describes a stock whose buyer does not receive the most recently declared dividend. Dividends are payable only to shareholders recorded on the books of the company as of a specific date of record (the "record date"). If you buy the stock any time after the record date for a particular dividend, you won't receive that dividend.

**EX-DIVIDEND DATE:** The day on and after which the buyer of a stock does not receive a particular dividend. This date is sometimes referred to simply as the "ex-date," and can apply to other situations beyond cash dividends, such as stock splits and stock dividends. On the ex-dividend date, the opening price for the stock will have been reduced by the amount of the dividend, but may open at any price due to market forces.

**EXECUTION:** The actual completion of an order to buy or sell stock or options.

**EXERCISE:** If the buyer of a stock option wants to buy (in the case of a call) or sell (in the case of a put) the underlying stock at the strike price or, in the case of a cash-settled option, to receive the index price and the strike price settlement amount, the option must be exercised. To exercise an option, a person who is long an option must give his broker instructions to exercise a particular option (or if the option is ¾ of a point in-the-money at expiration it will be automatically exercised for a customer) Someone with short option positions must be aware of the possibility of being assigned if his short options in-the-money, and he must make sure he has adequate buying power available in his account to cover any such potential assignment.

**EXERCISE PRICE (STRIKE PRICE):** The cost per share at which the holder of an option may buy or sell the underlying security. (NASD/Options)

**EXPIRATION CYCLE:** The expiration cycle has to do with the dates on which options on a particular underlying security expire. A stock option, other than LEAPS, will be in one of three cycles, the January cycle (with options listed in January, April, July or October), the February cycle (with options listed in the February, May, August or November) or the March cycle (with options listed in March, June, September or December). At any given time, an option will have contracts with four expiration dates outstanding.

**EXPIRATION (EXPIRATION DATE):** On the expiration date, an option and the right to exercise it cease to exist. Every option contract becomes null and void after its expiration date. For stock options, this date is the Saturday following the third Friday of the expiration month.

 

**EXTRINSIC VALUE (TIME VALUE):** The difference between the entire price of an option and its intrinsic value. For example, if a call option with a strike price of $50 has a price of $2.75, with the stock price at $52, the extrinsic value is $.75. The price of an out-of-the-money (OTM) option is made up entirely of extrinsic value.

**FAST MARKET:** The exchange declares trading in stocks or options to be in a "fast market" when transactions in the pit occur in such volume and with such rapidity that price reporters are behind in entering quotes. During this time, executing brokers are not held to any fills if a price is traded through on a limit order.

**FED FUNDS (FEDERAL FUNDS):** The money a bank borrows from another night to meet its overnight reserve requirements.

**FED FUNDS RATE:** Set by the Federal Reserve Board, the Fed Funds Rate is the rate banks charge each other on overnight loans held the Federal Reserve Bank.

**FEDERAL OPEN MARKET COMMITTEE (FOMC):** A committee of the Federal Reserve Board which operates by buying and selling government securities in the open market. This buying and selling is how the Federal Reserve Board controls the U.S. money supply. The FOMC decides whether to change the discount rate or not.

**FEDERAL RESERVE BOARD (FRB):** A seven-member board of governors of the Federal Reserve System, appointed by the U.S. President and confirmed by the Senate, that is responsible for monetary policy within the United States. It controls the supply of money and credit to try to control inflation and create a stable, growing economy.

**FENCE:** An option and stock position consisting of long stock, long an out-of-the-money put and short an out-of-the-money call, which emulates a bull spread. Alternatively, a reverse fence can be long stock, long in-the-money put and short in-the-money call which emulates a bear spread. All the options have the same expiration date.

**FILL:** The result of executing an order.

**FILL OR KILL (FOK):** A type of order that is canceled unless it is executed completely within a designated time period, generally as soon as it is announced by the floor broker to the traders in the pit. Compare to all-or-none (AON).

**FLAT:** Used to describe an account that has no open positions in stocks or options. Flat can also be regarding a position with little or no delta or gamma.

**FLOAT:** Number of shares of stock of a corporation that available for public trading.

**FLOOR:** Physical location of an exchange where the buying and selling of stocks or options takes place.

**FLOOR BROKER:** A member of an exchange who executes orders on the exchange floor for clearing members or their customers.
**FLOOR TRADER:** A member of an exchange who trades only for his own or proprietary account. On the CBOE, they are known as "market makers".

**FREE CREDIT BALANCE:** The amount of cash in a customers account. Broker-Dealers are required to notify customers of their free credit balances at least quarterly..

**FROZEN ACCOUNT:** An account which requiring cash in advance for a buy order to be executed or securities in hand before a sell order is executed. In most cases customers whose accounts are frozen will be restricted to closing transactions only. (NASD)

**FULL POWER OF ATTORNEY:** A written authorization for someone other than the beneficial owner of an account to execute trades, make deposits or withdrawals in a customer account. (NASD)

**FULL TRADING AUTHORIZATION:** An authorization, usually provided by a full power of attorney, which gives someone other than the customer full trading privileges in the account. (NASD)

**FUNDAMENTAL RESEARCH:** Analysis of companies based on such factors as revenues, expenses, assets, debt level, earnings, products, management, and various financial ratios. As is relates to the economy, fundamental research includes analysis of gross national product, interest rates, unemployment, savings, etc.

**FUNDAMENTALS:** Factors that are used to analyze a company and its potential for success, such as earnings, revenues, cash flow, debt level, financial ratios, etc.

 

**FUNGIBILITY:** Interchangeability resulting from identical characteristics or value. Options on a stock with the same expiration date, type (call or put) and strike price as standardized by the Options Clearing Corporation (OCC) are fungible. Therefore, dual-listed options traded on the CBOE can be liquidated or closed on the AMEX.

**FUTURE(S) CONTRACT:** A forward contract for the future delivery of a financial instrument (ex. Treasury bond) or physical commodities (corn), traded on a futures exchange (ex. CBOT, CME).

**GAMMA:** An approximation of the change in the delta of an option relative to a change in the price of the underlying stock when all other factors are held constant. Gamma is accurate for small changes in the price of the underlying stock, but is expressed in terms of a change in delta for a 1 point move in the stock. For example, if a call has a delta of .49 and a gamma of .03, if the stock moves down 1 point, the call delta would be .46 (.49 + (.03 x -$1.00)). Generated by a mathematical model, delta depends on the stock price, strike price, volatility, interest rates, dividends, and time to expiration.

**GOOD-TIL-CANCELED (GTC):** A type of limit order that is active until it is filled or canceled. As opposed to a day order, a GTC order can remain active for an indefinite number of trading sessions.

**GREEKS:** Regarding options, it's a colloquial term for the analytic measurements such as delta, gamma, theta, vega and rho, etc.

**HANDLE:** The whole-dollar part of the bid or offer price. For example, if the bid and offer prices for an option are 3 1/8 bid, offer 3/1/2, the handle is 3.

**HEDGE:** A position in stock or options that is established to offset the risk of another position in stock or options.

**HIGH (H):** In reference to the O,H,L,C, "H" represents the high price of the session.

**HISTORICAL VOLATILITY:** The annualized standard deviation of percent changes in the price of a stock over a specific period. Compare to implied volatility.

**HOLDER:** Someone who has bought an option or owns a security.

**HYPOTHECATION:** The act of pledging of securities as collateral, as might be done in a margin account.

**IMMEDIATE OR CANCEL (IOC):** A type of order that must be filled immediately or be canceled. IOC orders allow partial fills, with the balance of the order canceled.

**IMPLIED VOLATILITY:** An estimate of the volatility of the underlying stock that is derived from the market value of an option. Implied volatility is the volatility number that, if plugged into a theoretical pricing model along with all the other inputs, would yield a theoretical value of an option equal to the market price of the same option. Compare to historical volatility.

**INDEX:** A proxy for the overall stock market or segments of the stock market. An index is typically made up of a group of stocks that are selected to represent all stocks in the stock market or market segment (such as technology stocks or big capitalization stocks). The performance of the index gives an idea of how individual stocks might be performing. The S&P 500 (Standard & Poor's 500) and Dow Jones Industrial Average are two well-known indices.

**INDEX OPTION:** An option that has a stock index as the underlying security. The value of an index option is based on the value of the index. Typically, index options are cash settled options.

**INITIAL MARGIN REQUIREMENT:** The amount of equity a customer must deposit when making a new purchase in a margin account. For retail customers the SEC 's Regulation T requirement for equity securities currently stands at 50% of the purchase price. In addition, the NASD and NYSE initial margin requirement is a deposit of $2,000 but not more than 100% of the purchase price. Purchases of options must be paid for in full while the sale of naked options is subject to house requirements. Also, the amount of money required to be in an account with a brokerage firm to carry a new position into the next trading day.

**INITIAL PUBLIC OFFERING (IPO):** A corporation's first sale of stock to the public.

**INSTITUTIONAL INVESTORS:** Organizations such as mutual funds, pension funds, endowment funds, and insurance companies that typically have very large sums of money to invest.

 

**INTEREST:** Money paid when borrowing money or money earned when lending money.

**INTEREST RATE:** A percentage that is charged when borrowing money, or that is earned when lending money.

**INTEREST RATE RISK:** Risk that a change in interest rates will cause a position to change in value.

**IN-THE-MONEY (ITM):** A call option is in-the-money when the price of the underlying stock is greater than the call's strike price. . Conversely, a put option is in-the-money when the price of the underlying stock is lower than the put's strike price. At expiration, options that are ¾ of a point ITM are automatically exercised.

**INTRINSIC VALUE:** Any positive value resulting from the stock price minus the strike price (for calls) or strike price minus the stock price (for puts). Only in-the-money options have intrinsic value, and intrinsic value can never be zero or less. For example, if a call option with a strike price of $50 has a price of $2.75, with the stock price at $52, the intrinsic value is $2.00. If a put option with a strike price of $15 has a price of $1.50, with the stock price at $14, the intrinsic value is $1.00. Compare to extrinsic value.

**INVESTOR:** Someone who purchases a stock with the intent of holding it for some amount of time and profiting from the transaction. Compare to day trading.

**IRON BUTTERFLY SPREAD:** An option spread composed of calls and puts, with long options and short options at three different strikes. The options are all on the same stock and of the same expiration, with the quantity of long options and the quantity of short options netting to zero. The strikes are equidistant from each other. An iron butterfly can be seen as a straddle at the middle strike and a strangle at the outer strikes. For example, a long 50/60/70 iron butterfly is long 1*50 put, short 1*60 call, short 1*60 put, and long 1*70 call. It's important to understand that you buy an iron butterfly for a credit, that is, you take money in when you buy it.

**IRON CONDOR SPREAD:** An option spread composed of calls and puts, with long options and short options at four different strikes. The options are all on the same stock and of the same expiration, with the quantity of long options and the quantity of short options netting to zero. Generally, the strikes are equidistant from each other, but if the strikes are not equidistant, the spread is called an iron pterodactyl. An iron condor can be seen as a strangle at the middle strike and a strangle at the outer strikes. For example, a long 50/55/60/65 iron condor is long 1*50 put, short 1*55 put, short 1*60 call, and long 1*65 call. It's important to understand that you buy an iron condor for a credit, that is, you take money in when you buy it.

**ISSUE:** As a verb, when a company offers shares of stock to the public; as a noun, the stock that has been offered by the company.

**ISSUER:** (1) An entity that offers or proposes to offer its securities for sale. (2) The creator of an option; the issuer of a listed option is the OCC.

**JOINT ACCOUNT:** An account that has two or more owners who possess some form of control over the account and these individuals may transact business in the account. See also joint tenants.

**JOINT TENANTS (JT):** A type of account with two owners. There are two types of joint tenant accounts: 1) Joint Tenants With Rights of Survivorship - in the event of the death of one party, the survivor receives total ownership of the account and 2) Joint Tenants in Common - in the event of the death of one party, the survivor receives a fractional interest of the account, the remaining fractional interest goes to the deceased party's estate.

**JUNK BOND (HIGH-YIELD BOND):** A bond with a credit rating of BB or lower, carrying higher risk of default than investment grade bonds.

**KEOGH PLAN:** Qualified retirement plan designed for employees of unincorporated businesses or persons who are self-employed, either full-time or part-time.

**KNOW YOUR CUSTOMER:** The industry rule that requires that each member organization exercise due diligence to learn the more essential facts about every customer.

**LAST (PRICE):** The price of the last transaction of a stock or option for a trading session.

**LAST TRADING DAY:** The last business day prior to the option's expiration date during which options can be traded. For equity options, this is generally the third Friday of the expiration month. Note: If the third Friday of the month is an exchange holiday, the last trading day will be the Thursday immediately preceding the third Friday.

 

**LEAPS:** An acronym for Long-term Equity AnticiPation Securities. LEAPS are call or put options with expiration dates set as far as two years into the future. They function exactly like other, shorter-term exchange-traded options.

**LEG(S) LEGGING:** A term describing one option of a spread position. When someone "legs" into a call vertical, for example, he might do the long call trade first and does the short call trade later, hoping for a favorable price movement so the short side can be executed at a better price. Legging is a higher-risk method of establishing a spread position, and RiskDoctor STRONGLY suggests that if you decide to leg into a spread, you should, for margin and risk purposes, do the long trades FIRST.

**LEVERAGE:** The ability to control of a larger amount of money or assets with a smaller amount of money or assets, typically done by borrowing money or using options. If prices move favorably for a leveraged position, the profits can be larger than on an unleveraged position. However, if prices move against a leveraged position, the losses can also be larger than on an unleveraged position, but not necessarily with an options position. Buying stock on margin is using leverage. A long option position is leveraged because it "controls" a large number of shares with less money than it would take to maintain a position with the same number of shares.

**LIMIT MOVE:** Relating to futures markets, a limit move is an increase or decrease of a futures price by the maximum amount allowed by the exchange for any one trading session. Price limits are established by the exchanges, and approved by the Commodity Futures Trading Commission (CFTC). Limit moves vary depending on the futures contract.

**LIMIT (PRICE) ORDER:** An order that has a limit on either price or time of execution, or both. Compare to a market order that requires the order be filled at the most favorable price as soon as possible. Limit orders to buy are usually placed below the current ask price. Limit orders to sell are usually placed above the current bid price. It is wise to use limit orders when trading spreads. In markets with low liquidity or in fast markets, some traders use limits to ensure getting filled by putting in a limit order to buy at or above the ask price or a limit order to sell at or below the bid price.

**LIMITED POWER OF ATTORNEY:** An authorization giving someone other than the beneficial owner of an account the authority to make certain investment decisions regarding transactions in the customers account.

**LIMITED TRADING AUTHORIZATION:** This authorization, usually provided by a limited power of attorney, grants someone other than the customer to have trading privileges in an account. These privileges are limited to purchases and sales; withdrawals of assets is not authorized.

**LIQUIDATION:** A transaction or transactions that offsets or closes out a stock or options position.

**LIQUIDITY:** The ease with which a transaction in stock or options can take place without substantially affecting their price.

**LIQUIDITY RISK:** The potential that an investor might not be able to buy or sell a security when desired.
**LISTED OPTIONS:** An exchange-approved call or put traded on an options exchange with standardized terms. Listed options are fully fungible. In contrast, over-the-counter (OTC) options usually have non-standard or negotiated terms.

**LISTED STOCK:** The stock of a corporation that is traded on a securities exchange.

**LOAN CONSENT AGREEMENT:** The agreement between a brokerage firm and its margin customer permitting the brokerage firm to lend the margined securities to other brokers; this contract is part of the margin agreement.

**LOAN VALUE:** The maximum amount of money that can be borrowed in a margin account at a brokerage firm using eligible securities as collateral.

**LOCAL:** A term for a trader at the CBOT or CME who trades for his own account. They compete with each other to provide the best bid and ask prices for futures. Locals are basically the same type of traders that market makers are at the CBOE.

**LOCKED LIMIT:** Refers to a futures market that has moved its daily maximum amount and, if the move is up, no one is willing to sell. Conversely, if the move is down, no one is willing to buy. Hence, the market is “locked” at the limit price with no trading.

 

**LONG:** As a noun, it refers to people who have bought stock or options. As an adjective, it refers to a position of long stock or options. Compare to short.

**LONG HEDGE:** The strategy of buying puts as protection against the decline in the value of long securities.

**LONG MARKET VALUE (LMV):** See Current Market Value.

**LOT:** Contract

**LOW (L):** In reference to the O,H,L,C, "L" represents the low price of the session.

**MAINTENANCE MARGIN:** An amount of cash or margin-eligible securities that must be maintained on deposit in a customer's account to maintain a particular position. If a customer's equity in his account drops to, or under, the maintenance margin level, the account may be frozen or liquidated until the customer deposits more money or margin-eligible securities in the account to bring the equity above the maintenance margin level.

**MARGIN:** The amount of equity contributed by a customer (in the form of cash or margin-eligible securities) as a percentage of the current market value of the stocks or option positions held in the customer's margin account.

**MARGIN ACCOUNT:** An account that allows a customer to borrow money from a brokerage firm against cash and margin-eligible securities held in the customer's margin account at that brokerage firm.

**MARGIN BALANCE:** The amount a customer has borrowed, using cash or margin-eligible securities as collateral, in his margin account.

**MARGIN CALL:** A brokerage firm's demand of a customer for additional equity in order to bring margin deposits up to a required minimum level. If the customer fails to deliver more equity in the account, the customer's positions may be liquidated.

**MARGIN-ELIGIBLE SECURITIES:** Securities, such as stocks or bonds, that can be used as collateral in a margin account. Options are not margin-eligible securities.

**MARGIN REQUIREMENT:** The minimum equity required in an account to initiate or maintain a position in stock or options.

**MARKET:** 1) A quote, that is a bid and ask price for a stock or option, ex. the market on the XYZ Dec 75 calls is 2 ½ - 3, or 2) a term for all stocks as a whole, ex. the market is going up means stocks in general are rising, or 3) a place to trade.

**MARKET ARBITRAGE:** The simultaneous purchase and sale of the same security in different markets to take advantage of price disparity between the two markets. For example, purchasing a call or put on the CBOE subsequently selling the contract at the PHLX at a higher price.

**MARKET IF TOUCHED (MIT):** A type of stock order that becomes a market order when a particular price on a stock is reached. A buy MIT order is placed below the market; a sell MIT order is placed above the market.

**MARKET MAKER:** A term for a trader at the CBOE or PCX who trades for his own account. They compete with each other to provide the best bid and ask prices for options to the public.

**MARKET ON CLOSE (MOC):** An order to buy or sell stock or options at the end of the trading session at a price within the closing range of prices. MOC orders must be placed 45 minutes before the close of trading.

**MARKET (PRICE) ORDER:** An order to buy or sell stock or options that is to be executed as soon as possible at the best possible price. Compare to a limit order or stop order, which specifies requirements for price or time of execution.

**MARK-TO-MARKET:** The daily updating of the value of stocks and options to reflect profits and losses in a margin account.

**MARRIED PUT:** The purchase of a put option and the underlying stock on the same day. Special tax rules may apply to this position.

**MERGER:** The act of combining two or more corporations into one corporate entity. Options on stocks involved in mergers can be difficult to evaluate.

 

**MINIMUM PRICE FLUCTUATION:** The smallest possible increment of price movement for a stock or option. It is often referred to as a "tick".

**MODEL:** Any one of the various option pricing models used to value options and calculate the "Greeks". Models typically use six factors in their calculations: the underlying stock price, the strike price, the time until expiration, dividends, interest rates, and the volatility of the stock. RiskDoctor uses the Black-Scholes model for European-style options, and the Binomial model for American-style options.

**MONEY MARKET FUND:** A special type of mutual fund that invests only in short-term, low-risk fixed-income securities, such as bankers' acceptances, commercial paper, repurchase agreements and Treasury bills. The money market fund manager tries to maintain a share price of $1.00. Money market funds are not federally insured, even though the money market fund's portfolio may consist of guaranteed securities.

**MULTIPLE LISTED:** When the same stock or option is listed on two or more different exchanges. For example, IBM options are traded on the CBOE, PHLX and AMEX.

**MULTIPLIER:** Refers to the number, typically $100, used to calculate aggregate strike prices and premiums for options. The multiplier affects profit/loss calculations on options positions.

**NAKED CALL OR PUT:** Refers to a short option position that doesn't have an offsetting stock position. For example, a customer has a naked call if he sells a call without being long the quantity of stock represented by his short call or a long another call spread against it. He has a naked put if he sells a put without being short the quantity of stock represented by his short put or long another put spread against it. Compare to covered call or put.

**NATIONAL ASSOCIATION OF SECURITIES DEALERS** (**NASD**): Is an association of brokers and dealers in the over-the-counter (OTC) stock business.

**NATIONAL ASSOCIATION OF SECURITIES DEALERS AUTOMATIC QUOTATION SYSTEM (NASDAQ):** An electronic information network that provides price quotations to brokers and dealers for the more actively traded common stock issues in the OTC market. There are three levels to the NASDAQ. Level I shows highest bid and lowest ask prices in the system for an OTC stock. Level II shows individual OTC stock market maker's quotes for an OTC stock. Level III is used by OTC stock market makers to enter their quotes into the NASDAQ system.

**NET CHANGE:** The change in the price of a stock or option from the closing price of the previous day.

**NET POSITION:** The difference between a customer's open long and open short positions in any one stock or option.

**NEW YORK STOCK EXCHANGE (NYSE):** Founded in 1792, it is the oldest and largest stock exchange in the United States. Options are not traded on the NYSE.

**NOMINAL OWNER:** The role of a brokerage firm when customer securities are held in street name.

**NON-MARGIN SECURITY:** Security that must be paid for in full. Call and put option contracts are examples of this type of security.

**NOT HELD ORDER (NH):** An order that gives the floor broker discretion on time and price in getting the best possible fill for a customer. When entering a not held order, a customer agrees to not hold the broker responsible if the best price is in not obtained.

**NUMBERED ACCOUNT:** This account is titled with something other than the account holder's name (for example-symbols or numbers). To open this type of account the customer usually must sign a form designating ownership of the account.

**ODD LOT:** The purchase or sale of stock in less than the round lot increment of 100 shares.

**OEX:** OEX is the symbol for the Standard & Poor's 100 cash Index. It is a capitalization-weighted index of 100 stocks from a broad range of industries. Cash-settled, American-style options on the OEX are traded at the CBOE.

**OFFER:** Another name for the ask price. The price of a stock or option at which a seller is offering to sell.

**ONE CANCELS OTHER (OCO):** Two orders submitted simultaneously by one customer, where if one order is filled, the other is canceled immediately. A type of order which treats two or more option orders as a package, whereby the execution of any one of the orders causes all the orders to be reduced by the same amount. For example, the investor would enter an OCO order if he/she wished to buy 10 May 60 calls or 10 June 60 calls or any combination of the two which when summed equaled 10 contracts. An OCO order may be either a day order or a GTC order.

**OPEN (O), THE:** The beginning of the trading session. In reference to the O,H,L,C, “O” represents the opening price of the session.

**OPEN EQUITY**. The value of all open positions in stock and options, less the margin requirements of those positions.

**OPEN INTEREST:** The number of outstanding option contracts in a particular class or series. Each opening transaction (as opposed to a closing transaction) has a buyer and a seller, but for the calculation of open interest, only one side of the transaction is counted.
**OPEN (PRICE) ORDER:** An order that is active until it is either executed or canceled.

**OPEN OUTCRY:** A public auction, using verbal bids and offers, for stocks or options on the floor of an exchange.

**OPEN POSITION:** A long or short position in stock or options.

**OPENING PRICE/RANGE:** The range of the first bid and offer prices made or the prices of the first transactions.

**OPENING ROTATION:** Process by which options are systematically priced after the opening of the underlying stock.

**OPENING TRADE/TRANSACTION:** An opening purchase transaction adds long stock or options to a position, and an opening sale transaction adds short stock or options to a position.

**OPTION:** A call or a put, an option is a contract that entitles the buyer to buy (in the case of a call) or sell (in the case of a put) a number of shares of stock at a predetermined price (strike price) on or before a fixed expiration date.

**OPTION CHAIN:** A list of all options on a particular stock.

**OPTION CLASS:** See CLASS OF OPTIONS

**OPTION PRICING MODEL:** Any one of the various models used to value options and calculate the "Greeks". Models typically use six factors in their calculations: the underlying stock price, the strike price, the time until expiration, dividends, interest rates, and the volatility of the stock. RiskDoctor uses the Black-Scholes model for European-style options, and the Binomial model for American-style options.

**OPTIONS CLEARING CORPORATION, THE (OCC):** The issuer and registered clearing facility of all options contracts traded on the AMEX, CBOE, PCX, and PHLX. It supervises the listing of options and guarantees performance on option contracts.

**OPTIONS DISCLOSURE DOCUMENT:** This document is published by The Options Clearing Corporation (OCC) and must be distributed to all customers intending to open an option account.. The document itself outlines the risks and rewards of investing in options. The document is also called the OCC Risk Disclosure Document.
**ORDER:** An instruction to purchase or sell stock or options.

**ORDER BOOK OFFICIAL (OBO):** Employees of the exchanges, OBOs manage customers' limit orders on the floor of the exchange.

**ORDER FLOW:** The orders to buy and sell stock or options that brokers send to market makers.

**ORDER ROUTING SYSTEM (ORS):** The system utilized by the Chicago Board Options Exchange (CBOE) to collect, store, route and execute orders for customers of the exchange. The ORS system automatically routes option market and limit orders to the various execution vehicles at the CBOE including the RAES system.

**OTC OPTION:** Options traded in the OTC market. OTC options are not listed on or guaranteed an options exchange and do not have standardized terms, such as standard strike prices or expiration dates. (see Fungibility).

**OUT-OF-THE-MONEY (OTM):** A call is out-of-the-money when the price of the underlying stock is lower than the call's strike price. A put is out-of-the-money when the price of the underlying stock is higher than the put's strike price. Out-of-the-money options have zero intrinsic value.

**OUT-TRADE(S):** A situation that results when there is some error on a trade. Differences between the buyer and seller regarding option price, option strike price or expiration month, or underlying stock are some of the reasons an out-trade might occur. Other costly errors occur when there was a buy versus a buy or a sell versus a sell.

**OVER-THE-COUNTER (OTC) MARKET:** A securities market made up of dealers who may or may not be members of a securities exchange. In the OTC market, there is no exchange floor, such as the NYSE or CBOE.

**PACIFIC EXCHANGE (PCX):** Located in San Francisco, the PCX is one of four U.S. exchanges that trade equity options.

**PARITY:** A term used to describe an in-the-money option when the option's total premium is equal to its intrinsic value. Such an option moves 1 point for every 1 point move in the underlying stock, and is said to be "worth parity" or "trading for parity".

**PARTIAL FILL:** A limit order that is only partially executed because the total specified number of shares of stock or options could not be bought or sold at the limit price.

**PAYABLE DATE:** Date on which the dividend on a stock is actually paid to shareholders of record. Compare to ex-dividend date and record date.

**PHILADELPHIA STOCK EXCHANGE (PHLX):** Located in Philadelphia, the PHLX is one of four U.S. exchanges that trade equity options.

**PIN RISK:** The risk to a trader who is short an option that, at expiration, the underlying stock price is equal to (or "pinned to") the short option's strike price. If this happens, he will not know whether he will be assigned on his short option. The risk is that the trader doesn't know if he will have no stock position, a short stock position (if he was short a call), or a long stock position (if he was short a put) on the Monday following expiration and thus be subject to an adverse price move in the stock.

**PLUS TICK or UP TICK:** A term used to describe a trade made at a price higher than the preceding trade.

**PLUS TICK RULE:** SEC regulation governing the market price at which a short sale may be made. Meaning, no short sale may be executed at a price below the price of the last sale. See also down tick or minus tick.

**POINT:** The minimum change in the handle of a stock or option price. For stock or options in the U.S., a point means $1. If the price of an option goes from $2.00 to $7.00, it has risen 5 points.

**POSITION:** Long or short stock or options in an account.

**POSITION LIMIT:** For a single trader, customer, or firm, the maximum number of allowable open option contracts on the same underlying stock. The limits are established by the exchanges.

**POSITION TRADING:** Establishing a position in stocks or options and holding it for an extended period of time. Compare to day trading.

**PREFERRED STOCK:** A class of stock (as distinguished from common stock) with a claim on a company's earnings before dividends may be made on the common stock. Preferred stock usually has priority over common stock if the company is liquidated.

**PREMIUM:** The price of an option.

**PRIME RATE:** The lowest interest rate commercial banks charge their largest and most credit-worthy corporate customers.

**PUT OPTION:** A put option gives the buyer of the put the right, but not the obligation, to sell the underlying stock at the option's strike price. The seller of the put is obligated to take delivery of (buy) the underlying stock at the option's strike price to the buyer of the put when the buyer exercises his right.

**QUOTE:** The bid to buy and the offer to sell a particular stock or option at a given time. If you see a "quote" for an option on the screen "3 ½ - 3 $^{7}/_{8}$", it means that the bid price is $3.50 and the ask price is $3.875. This means that at the time the quote was disseminated, $3.50 was the highest price any buyer wanted to pay, and $3.875 was the lowest price any seller would take.

**RALLY:** A rise in the price of a stock or the market as a whole. Compare to reaction.

**RANGE:** The high and low prices of a stock or option recorded during a specified time.

 

**RATIO SPREAD:** An option position composed of either all calls or all puts, with long options and short options at two different strike prices. The options are all on the same stock and usually of the same expiration, with more options sold than purchased. A ratio spread is the purchase of an option(s) and the sale of a greater number of the same type of options that are out-of-the-money with respect to the one(s) purchased. For example, a 50/60 call 1-by-2 ratio spread is long 1*50 call and short 2*60 calls.

**REACTION:** A decline in price of a stock or the market as a whole following a rise. Compare to rally.

**REALIZED GAINS OR LOSSES:** The profit or loss incurred in an account when a closing trade on a stock or option is made and matched with an open position in the same stock or option.

**RECORD DATE (DATE OF RECORD):** The date by which someone must be registered as a shareholder of a company in order to receive a declared dividend. Compare to ex-dividend date and payment date.

**REGISTERED OPTIONS PRINCIPAL:** An employee of a brokerage firm who has passed the NASD Series 4 exam, which provides in-depth knowledge related to options. The registered options principal is an officer or partner in a brokerage firm who approves customer accounts in writing.

**REGISTERED REPRESENTATIVE:** An employee of a brokerage firm who has passed the NASD Series 7 and Series 63 exam.

**REGULATION T (REG T):** The regulation, established by the Federal Reserve Board, governing the amount of credit that brokers and dealers may give to customers to purchase securities. It determines the initial margin requirements and defines eligible, ineligible, and exempt securities.

**REHYPOTHECATION:** The practice of pledging a customer's securities as collateral for a bank loan. A brokerage firm may rehypothecate up to 140% of the value of their customers' securities to finance margin loans to customers.

**REJECTED ORDER:** An order that is not executed because it is invalid or unacceptable in some way.

**RESTRICTED ACCOUNT:** A margin account in which the equity is less than the REG-T initial requirement. A restricted account will be restricted to closing transactions only.

**RETAIL AUTOMATIC EXECUTION SYSTEM (RAES):** The system utilized by the CBOE to execute option market and executable limit orders for retail customers received by the exchange's ORS. Retail option orders executed via the RAES system are filled instantaneously at the prevailing market quote and are confirmed almost immediately to the originating firm.

**REVERSAL (MARKET REVERSAL):** When a stock's direction of price movement stops and heads in the opposite direction.

**REVERSAL (REVERSE CONVERSION):** A position of short stock, long a call, and short a put (with the call and put having the same strike price, expiration date, and underlying stock). The long call and short put acts very much like long stock, thus acting as a hedge to the short stock. So, a reversal has a very small delta. A reversal is a way to exploit mispricings in carrying costs.

**REVERSE SPLIT:** An action taken by a corporation in which the number of outstanding shares is reduced and the price per share increases. For example, if a trader were long 100 shares of stock of a company with a price of $80, and that company instituted a 1-for-4 reverse split, the trader would see his position become long 25 shares of stock with a price of $320. The value of the trader's position does not change (unless the price of the stock subsequently changes) and his proportionate ownership in the company remains the same. Compare to stock split.

**RHO:** An approximation of the change in the price of an option relative to a change in interest rates when all other factors are held constant. This is typically expressed for a one-percent (100 basis point) change in interest rates. For example, if a call has a price of $4.00 and a rho of 0.2, if interest rates rise 1%, the call would have a price of $3.8 ($4.00 – (.2 x 1.00)). Generated by a mathematical model, rho depends on the stock price, strike price, volatility, interest rates, dividends, and time to expiration.

**ROLL, THE:** An option spread position composed of both calls and puts. The options are all on the same stock and strike price, but on two expirations. The roll is long synthetic stock (long call, short put) at one expiration and short synthetic stock (short call, long put) at another expiration. The quantity of long options and the quantity of short options net to zero. For example, short the SEP/DEC 70 roll is long 1 September 70 call, short 1 September 70 put, short 1 December 70 call, and long 1 December 70 put. The roll is usually executed when someone wishes to roll from a hedge in an expiring month to a hedge in a deferred month for added time.

**ROLL, TO:** Adjusting or changing a position by closing out an existing option position and substituting it with an option on the same stock but with a different strike price or expiration date.

**ROUND LOT:** A standard quantity of trading. For example, in U.S. equities, a round lot is 100 shares of stock.

**SCALP:** A quick entry and exit on a position.

**SCALPER/SCALPING:** Someone who enters and exits stock or options positions quickly, with small profits or losses, holding a position only for a short time during a trading session.

**SEAT:** A name for a membership on an exchange.

**SECONDARY MARKET:** Markets in which securities are bought and sold subsequent to their being sold to the public for the first time.

**SECURITIES AND EXCHANGE COMMISSION (SEC):** A government agency established by Congress to help protect investors. The SEC regulates the stock, stock options, and bond markets.

**SECURITIES INVESTOR PROTECTION CORPORATION (SIPC):** This is a nonprofit corporation created by an act of congress to protect clients of a brokerage firms that are forced into bankruptcy. SIPC provides customers of these firms up to $500,000 coverage for cash and securities held by the firms, however, of that $500,000 only $100,000 in cash is covered.

**SECURITY:** A generic term for investment or trading vehicles. Securities can be stock, bonds, or derivative securities such as options or futures.

**SEGREGATION:** The holding of customer-owned securities separate from securities owned by other customers and securities by the brokerage firm.

**SELF REGULATORY ORGANIZATION (SRO):** Organizations accountable to the SEC for the enforcement of federal securities laws and the supervision of securities practices within their assigned fields of jurisdiction. Examples of these organizations are: NASD, NYSE and the CBOE.

**SERIES:** All option contracts of the same class that also have the same exercise price and expiration date.

**SETTLEMENT:** The conclusion of a stock or options trade through the transfer of the security (from the seller) or cash (from the buyer).

**SETTLEMENT DATE:** Date on which a transaction must be settled. Buyers pay for securities with cash and sellers deliver securities.

**SETTLEMENT PRICE:** The closing price of a stock or option used for account statements and to calculate gains and losses in an account.
**SHARES:** Stock.

**SHORT:** As a noun, it refers to people who have sold stock or options without owning them first. As an adjective, it refers to a position of short stock or options. Compare to long.

**SHORT COVERING:** Buying stock or options to close out a short position.

**SHORT HEDGE:** The selling of options as protection against a decrease in value of a long securities position.

**SHORT INTEREST:** The number of shares of stock that have been sold short is known as a stock's short interest.

**SHORT SELLER:** Someone who sells stock or options without owning them first. The short seller looks to profit from buying the stock or options back later at a price lower than where he sold it.

**SHORT SQUEEZE:** When traders who have sold a stock short start to lose profits or incur losses as the stock begins to rise, sometimes dramatically. The short sellers are forced to buy back their short stock positions in order to limit their losses.

**SINGLE ACCOUNT:** An account type in which only one individual has control over the investments and may transact business.

**SKEW:** See volatility skew.

**SKIP-STRIKE-FLY:** Butterfly configuration with a skipped strike. The result is a convoluted butterfly with many baby butterflies embedded within.

**SLINGSHOT, SLINGSHOTHEDGE™:** Position that behaves like a butterfly and an extra call and/or extra put. It can be performed with options only or with the underlying included.

**SLIPPAGE:** The difference between the price someone might expect to get filled at on an order, and the actual, executed price of the order.

**SPECIAL MEMORANDUM ACCOUNT (SMA):** A line of credit in a customer's margin account, it's a limit on the amount of money a customer can borrow against collateral in the account.

**SPECIALIST:** Members of the NYSE, PHLX, and AMEX whose function is to maintain a fair and orderly market by managing the limit order book and making bids and offers in a particular stock or class of options.

**SPECULATOR:** Someone who buys or sells stocks or options hoping to profit from favorable moves in their price or volatility. Generally, a speculator does not hedge his positions.

**SPIN-OFF:** When a corporation divides its assets into two companies, one the original company and the other a new, independent company. Shares of stock in the new company are issued to stockholders of the original corporation.

**SPLIT:** An action taken by a corporation in which the number of outstanding shares is increased and the price per share decreases. For example, if a trader were long 100 shares of stock of a company with a price of $120, and that company instituted a 3-for-1 split, the trader would see his position become long 300 shares of stock with a price of $40. The value of the trader's position does not change (unless the price of the stock subsequently changes) and his proportionate ownership in the company remains the same. Compare to reverse split.

**SPREAD:** 1) a position or order involving two or more different options or stock and options (see leg), or 2) the difference between the bid and offer prices of a stock or option.

**SPREAD ORDER:** A type of order specifying two different option contracts on the same underlying security.

**SPX:** SPX is the symbol for the Standard & Poor's 500 cash index. It is a capitalization-weighted index of 500 stocks from a broad range of industries. Cash-settled, European-style options on the SPX are traded at the CBOE.

**"SPYDERS" (SPDR):** Standard & Poor's Depository Receipts are pooled investments that trade like a stock, and are designed to provide investment results that generally correspond to one of the Standard and Poor's indices.

**STATEMENT:** A summary of a brokerage account's activity and balances.

**STOCK:** Another name for equity, it is a security that represents ownership in a corporation.

**STOCK OPTIONS:** Calls or puts with the right to buy or sell individual stocks.

**STOP LIMIT (PRICE) ORDER:** A type of order that turns into a limit order to buy or sell stock or options when and if a specified price is reached. Stop limit orders to buy stock or options specify prices that are above their current market prices. Stop limit orders to sell stock or options specify prices that are below their current market prices.

**STOP (STOP LOSS) ORDER:** A type of order that turns into a market order to buy or sell stock or options when and if a specified "stop" price is reached. Stop orders to buy stock or options specify prices that are above their current market prices. Stop orders to sell stock or options specify prices that are below their current market prices.

**STRADDLE:** An option position composed of calls and puts, with both calls and puts at the same strike. The options are on the same stock and of the same expiration, and either both long or both short with the quantity of calls equal to the quantity of puts (with the exception of a ratioed straddle). For example, a long 50 straddle is long 1*50 call and long 1*50 put. A long straddle requires a large move in the stock price, an increase in implied volatility or both for profitability, while a short straddle performs well when the stock is in during a tight trading range, decreased implied volatility or both.

 RiskDoctor@RiskDoctor.com

**STRADDLE STRANGLE SWAP:** AKA Double Diagonal or Calendarized Iron WingSpread. Usually configured as short closer dated straddle or strangle protected by wider strike further dated strangle.

**STRANGLE:** An option position composed of calls and puts, with both out-of-the-money calls and out-of-the-money puts at two different strikes. The options are on the same stock and of the same expiration, and either both long or both short with the quantity of calls equal to the quantity of puts (with the exception of a ratioed strangle). For example, a short 50/70 strangle is short 1*50 put and short 1*70 call. A long strangle requires a large move, an increase in implied volatility or both for profitability, while a short strangle performs well during a tight trading range, decreased implied volatility or both.

**STREET NAME:** Securities held in the name of a brokerage firm on behalf of a customer. This is required for margin accounts, and facilitates delivery for stock transactions.

**STRIKE PRICE:** The pre-determined price at which underlying stock is purchased (in the case of a call) or sold (in the case of a put) when an option is exercised.

**SYMBOLS:** Every corporation whose stock is traded on the NYSE, AMEX or NASDAQ, and every option traded on the CBOE, AMEX, PHLX, or PCX is given a unique identification symbol of up to five letters. Generally, these symbols abbreviate the corporation's complete name and, in the case of options, their strike price, expiration date, and whether they are calls or puts.

**SYNTHETIC:** Creating a position that emulates another by combining at least two of calls, puts or stock that acts very much like a position of outright stock, calls or puts.

**SYNTHETIC LONG CALL:** An option position composed of long puts and long stock. The quantity of long puts equals the number of round lots of stock. For example, long 5 synthetic 70 calls at can be created by being long 5*70 puts and long 500 shares of stock.

**SYNTHETIC LONG PUT:** An option position composed of long calls and short stock. The quantity of long calls equals the number of round lots of stock. For example, long 8 synthetic 80 puts at can be created by being long 8*80 calls and short 800 shares of stock.

**SYNTHETIC LONG STOCK:** An option position composed of long calls and short puts on the same stock, strike price and expiration. The quantity of long options and the quantity of short options nets to zero. For example, long 500 shares of synthetic stock can be created by being long 5*70 calls and short 5*70 puts. See combo.

**SYNTHETIC SHORT CALL:** An option position composed of short puts and short stock. The quantity of short puts equals the number of round lots of stock. For example, short 3 synthetic 60 calls at can be created by being short 3*60 puts and short 300 shares of stock.

**SYNTHETIC SHORT PUT:** An option position composed of short calls and long stock. The quantity of short calls equals the number of round lots of stock. For example, short 4 synthetic 70 calls at can be created by being short 4*70 calls and long 400 shares of stock.

**SYNTHETIC SHORT STOCK:** An option position composed of short calls and long puts on the same stock, strike price and expiration. The quantity of long puts and the quantity of short calls nets to zero. For example, short 400 shares of synthetic stock can be created by being short 4*70 calls and long 4*70 puts. See combo.

**SYSTEMATIC RISK:** The broad macroeconomic factors that affect all companies in a stock market. It is also known as market risk. Theoretically, it's the risk in a portfolio that cannot be reduced through diversification. Compare to unsystematic risk.

**TECHNICAL ANALYSIS:** Calculations that use stock price and volume data to identify patterns helping to predict future stock movements. Some technical analysis tool include moving averages, oscillators, and trendlines.

**TENDER OFFER:** An offer from one company to buy shares of stock of another company from that other company's existing stockholders. Those stockholders are asked to "tender" (surrender) their shares for a specific price (represented by cash, shares in another company, or both), which is usually higher than the current market price of the stock.

**THEORETICAL VALUE:** An estimated price of a call or put derived from a mathematical model, such as the Black-Scholes or binomial models.

**THETA:** An approximation of the decrease in the price of an option over a period of time when all other factors are held constant. Theta is generally expressed on a daily basis. For example, if a call has a price of $3.00 and a theta of 0.10, one day later, with all else unchanged, the call would have a price of $2.90 ($3.00 – (.10 x 1)). Generated by a mathematical model, theta depends on the stock price, strike price, volatility, interest rates, dividends, and time to expiration.

**TICK:** The smallest possible price increment for a stock or option.

**TICKER:** The telegraphic system which prints or displays last sale prices and volume of securities transactions on exchanges on a moving tape within a minute after each trade. Also known as the "tape".

**TIME AND SALES:** A record of the time, price and volume of each transaction of every stock and option.

**TIME DECAY:** Option price erosion over time. Another name for theta.

**TIME SPREAD:** Another name for calendar spread.

**TIME VALUE:** Another name for extrinsic value.

**TRADING AUTHORIZATION:** Written permission from the owner of an account authorizing another person to enter trades on behalf of the owner. Also called Power of Attorney.

**TRADING FLOOR:** The part of an exchange where the stocks and options are actually bought and sold.

**TRADING HALT:** A temporary suspension of trading in a particular stock due anticipation of a major news announcement or an imbalance of buy and sell orders.

**TRADING PIT:** A particular location on the trading floor of an exchange designated for the trading of a specific stock or options on a specific stock or index.

**TRANSFER AGENT:** Usually a division of a large bank or other financial institution that keeps records of the names of registered shareholders of a particular stock, the shareholders' addresses, the number of shares owned by each shareholder, and oversees the transfer of stock certificates from one shareholder to another.

**TREASURY STOCK:** Shares of stock issued by a company but later bought back by the company. These shares may be held in the company's treasury indefinitely, used for employee bonus plans, reissued to the public, or retired. Treasury stock is ineligible to vote or receive dividends.

**TREND:** Either an uptrend or a downtrend, successive price movements in the same direction in a security over time

**TRUST:** A legal relationship in which a person or entity (the trustee) acts for the benefit of someone else.

**TYPE:** The classification of an option as either a call or a put.

**UNCHED:** When the market is unchanged.

**UNCOVERED CALL OR PUT:** Another term for naked call or put.

**UNDERLYING (STOCK OR SECURITY):** The stock or other security that determines the value of a derivative security and that (with the exception of cash-settled options) would be purchased or sold if an option on that underlying stock or security was exercised. Examples of underlying securities are stocks, bonds, futures and indices.

**UNSYSTEMATIC RISK:** The company-specific microeconomic factors that affect an individual stock. Theoretically, it's the risk in a portfolio that can be reduced through diversification. Compare to systematic risk.

**UP-TICK:** A term used to describe a trade made at a price higher than the preceding trade.

**UPTREND:** Successive upward price movements in a security over time.

**VEGA:** An approximation of the change in the price of an option relative to a change in the volatility of the underlying stock when all other factors are held constant. This is typically expressed for a one-percent change in volatility. For example, if a call has a price of $2.00 and a vega of .65, if volatility rises 1%, the call would have a price of $2.65 ($2.00 + (.65 x 1.00)). Generated by a mathematical model, vega depends on the stock price, strike price, volatility, interest rates, dividends, and time to expiration.

 

**VERTICAL:** An option position composed of either all calls or all puts, with long options and short options at two different strikes. The options are all on the same stock and of the same expiration, with the quantity of long options and the quantity of short options netting to zero. A long call vertical (bull spread) is created by buying a call and selling a call with a higher strike price. A short call vertical (bear spread) is created by selling a call and buying a call with a higher strike price. A long put vertical (bear spread) is created by buying a put and selling a put with a lower strike price. A short put vertical (bull spread) is created by selling a put and buying a put with a lower strike price. For example, a short 70/80 put vertical is long 1*70 put and short 1*80 put.

**VIX (VOLATILITY INDEX):** Created by the CBOE, the VIX is an index of volatility calculated from the implied volatility of the OEX index options.

**VOLATILITY:** Generically, volatility is the size of the changes in the price of the underlying security. In practice, volatility is presented as either historical or implied.

**VOLATILITY SKEW:** Volatility skew, or just “skew”, arises when the implied volatilities of options in one month on one stock are not equal across the different strike prices. For example, there is skew in XYZ April options when the 80 strike has an implied volatility of 45%, the 90 strike has an implied volatility of 47%, and the 100 strike has an implied volatility of 50%. If the implied volatilities of options in one month on one stock ARE equal across the different strike prices, the skew is said to be “flat”. You should be aware of volatility skew because it can dramatically change the risk of your position when the price of the stock begins to move.

**VOLUME:** The total number of shares of stock or option contracts traded on a given day.

**WARRANT:** A security issued by a corporation that gives the holder the right to purchase securities at a specific price within a specified time limit (or sometimes with no time limit). Warrants are sometimes like call options, but the main differences are that warrants typically have much longer lives whereas options tend to expire relatively soon, and that warrants are issued by a company to raise money whereas options are created by the OCC.

**WRITE/WRITER:** An individual who sells an option short.