

§ 1.1092(c)-3

can be written is the next higher strike price, or \$15.00. This \$15.00 strike price requirement for a qualified covered call option applies to equity options with flexible terms, equity options with standardized terms, and qualifying over-the-counter options.

Example 3. Taxpayer owns stock in Corporation Z. On May 8, 2003, Taxpayer writes a 21-month equity call option with flexible terms on Corporation Z stock through a national securities exchange. The applicable stock price for Corporation Z stock is \$100. The bench marks for a 21-month equity option with standardized terms with an applicable stock price of \$100 will be based upon the adjusted applicable stock price. Using the table at §1.1092(c)-4(e), the applicable stock price of \$100 is multiplied by the adjustment factor 1.12, resulting in an adjusted applicable stock price of \$112. The highest available strike price less than the adjusted applicable stock price is \$110, and the second highest strike price less than the adjusted applicable stock price is \$105. Therefore, a 21-month equity call option with flexible terms on Corporation Z stock will not be deep in the money if the strike price is not less than \$105.

(d) *Effective date*—(1) *In general.* Except as provided in paragraph (d)(2) of this section, this section applies to equity options with flexible terms entered into on or after January 25, 2000.

(2) *Effective date for paragraphs (b) and (c) of this section.* Paragraphs (b) and (c) of this section apply to equity options with flexible terms entered into on or after July 29, 2002.

[T.D. 8866, 65 FR 3813, Jan. 25, 2000; Redesignated at 67 FR 20899, Apr. 29, 2002]

§ 1.1092(c)-3 **Qualifying over-the-counter options.**

(a) *In general.* Under section 1092(c)(4)(B)(i), an equity option is not a qualified covered call option unless it is traded on a national securities exchange that is registered with the Securities and Exchange Commission or other market that the Secretary determines has rules adequate to carry out the purposes of section 1092(c)(4). In accordance with section 1092(c)(4)(H), this requirement is modified as provided in paragraph (b) of this section.

(b) *Qualified covered call option status.* A qualifying over-the-counter option, as defined in §1.1092(c)-4(c), is a qualified covered call option if it meets the requirements of §§1.1092(c)-1 and 1.1092(c)-2(c) after using the language “qualifying over-the-counter option”

in place of “equity option with flexible terms”. For purposes of this paragraph (b), a qualifying over-the-counter option is deemed to satisfy the requirements of section 1092(c)(4)(B)(i).

(c) *Effective date.* This section applies to qualifying over-the-counter options entered into on or after July 29, 2002.

[67 FR 20900, Apr. 29, 2002]

§ 1.1092(c)-4 **Definitions.**

The following definitions apply for purposes of §§1.1092(c)-1 through 1.1092(c)-3:

(a) *Equity option with flexible terms* means an equity option—

(1) That is described in any of the following Securities Exchange Act Releases—

(i) Self-Regulatory Organizations; Order Approving Proposed Rule Changes and Notice of Filing and Order Granting Accelerated Approval of Amendments by the Chicago Board Options Exchange, Inc. and the Pacific Stock Exchange, Inc., Relating to the Listing of Flexible Equity Options on Specified Equity Securities, Securities Exchange Act Release No. 34-36841 (Feb. 21, 1996); or

(ii) Self-Regulatory Organizations; Order Approving Proposed Rule Changes and Notice of Filing and Order Granting Accelerated Approval of Amendment Nos. 2 and 3 to the Proposed Rule Change by the American Stock Exchange, Inc., Relating to the Listing of Flexible Equity Options on Specified Equity Securities, Securities Exchange Act Release No. 34-37336 (June 27, 1996); or

(iii) Self-Regulatory Organizations; Order Approving Proposed Rule Change and Notice of Filing and Order Granting Accelerated Approval of Amendment Nos. 2, 4 and 5 to the Proposed Rule Change by the Philadelphia Stock Exchange, Inc., Relating to the Listing of Flexible Exchange Traded Equity and Index Options, Securities Exchange Act Release No. 34-39549 (Jan. 23, 1998); or

(iv) Any changes to the Security Exchange Act Releases described in paragraphs (a)(1)(i) through (iii) of this section that are approved by the Securities and Exchange Commission; or

(2) That is traded on any national securities exchange that is registered

with the Securities and Exchange Commission (other than those described in the Security Exchange Act Releases set forth in paragraph (a)(1) of this section) and is—

(i) Substantially identical to the equity options described in paragraph (a)(1) of this section; and

(b) *Equity option with standardized terms* means an equity option—

(1) That is traded on a national securities exchange registered with the Securities and Exchange Commission;

(2) That, on the date the option is written, expires on the Saturday following the third Friday of the month of expiration;

(3) That has a strike price that is set at a uniform minimum strike price interval, that is established by the applicable national securities exchange registered with the Securities and Exchange Commission, and that is not less than \$1.00; and

(4) That has stock in a single corporation as its underlying security.

(c) *Qualifying over-the-counter option* means an equity option that—

(1) Is not traded on a national securities exchange registered with the Securities and Exchange Commission; and

(2) Is entered into with—

(i) A broker-dealer, acting as principal or agent, who is registered with the Securities and Exchange Commission under section 15 of the Securities Act of 1934 (15 U.S.C. 78a through 78mm) and the regulations thereunder and who must comply with the record-keeping requirements of 17 CFR 240.17a-3; or

(ii) An alternative trading system under 17 CFR 242.300 through 17 CFR 242.303; or

(iii) A person, acting as principal or agent, who must comply with the recordkeeping requirements for securities transactions described in 12 CFR 12.3, 12 CFR 208.34, or 12 CFR 344.4.

(d) *Single fixed strike price* means a strike price that is fixed, determinable, and stated as a dollar amount on the date the option is written. An option will not fail to have a single fixed strike price if, after the date the option is written, the strike price is adjusted to account for the effects of a dividend, stock dividend, stock distribution, stock split, reverse stock split, rights

offering, distribution, reorganization, recapitalization, or reclassification with respect to the underlying security, or a merger, consolidation, dissolution, or liquidation of the issuer of the underlying security.

(e) *Adjusted applicable stock price* means the applicable stock price, as defined in section 1092(c)(4)(G), adjusted for time. To determine the adjusted applicable stock price, the applicable stock price, which is determined in accordance with the rules in section 1092(c)(4)(G), is multiplied by an adjustment factor. The adjustment factor table is as follows:

Option term (in months)		Adjustment factor
Greater than	Not more than	
12	15	1.08
15	18	1.10
18	21	1.12
21	24	1.14
24	27	1.16
27	30	1.18
30	33	1.20

(f) *Securities Exchange Act Release* means a release issued by the Securities and Exchange Commission. To determine identifying information for releases referenced in paragraph (d)(1) of this section, including release titles, identification numbers, and issue dates, contact the Office of the Secretary, Securities and Exchange Commission, 450 5th Street, NW., Washington, DC 20549. To obtain a copy of a Securities Exchange Act Release, submit a written request, including the specific release identification number, title, and issue date, to Securities and Exchange Commission, Attention Public Reference, 450 5th Street, NW., Washington, DC 20549.

(g) *Effective dates.* (1) Except for paragraph (a)(2) of this section, paragraph (a) of this section applies to equity options with flexible terms entered into on or after January 25, 2000. Paragraph (a)(2) of this section applies to equity options with flexible terms entered into on or after July 29, 2002.

(2) Paragraphs (b), (c), (d), and (e) of this section apply to equity options entered into on or after July 29, 2002.

(3) Paragraph (f) of this section applies to equity options entered into on or after January 25, 2000.

[67 FR 20900, 20901, Apr. 29, 2002]

§ 1.1092(d)-1 Definitions and special rules.

(a) *Actively traded.* Actively traded personal property includes any personal property for which there is an established financial market.

(b) *Established financial market*—(1) *In general.* For purposes of this section, an established financial market includes—

(i) A national securities exchange that is registered under section 6 of the Securities Exchange Act of 1934 (15 U.S.C. 78f);

(ii) An interdealer quotation system sponsored by a national securities association registered under section 15A of the Securities Exchange Act of 1934;

(iii) A domestic board of trade designated as a contract market by the Commodities Futures Trading Commission;

(iv) A foreign securities exchange or board of trade that satisfies analogous regulatory requirements under the law of the jurisdiction in which it is organized (such as the London International Financial Futures Exchange, the Marche a Terme International de France, the International Stock Exchange of the United Kingdom and the Republic of Ireland, Limited, the Frankfurt Stock Exchange, and the Tokyo Stock Exchange);

(v) An interbank market;

(vi) An interdealer market (as defined in paragraph (b)(2)(i) of this section); and

(vii) Solely with respect to a debt instrument, a debt market (as defined in paragraph (b)(2)(ii) of this section).

(2) *Definitions*—(i) *Interdealer market.* An interdealer market is characterized by a system of general circulation (including a computer listing disseminated to subscribing brokers, dealers, or traders) that provides a reasonable basis to determine fair market value by disseminating either recent price quotations (including rates, yields, or other pricing information) of one or more identified brokers, dealers, or traders or actual prices (including rates, yields, or other pricing information) of recent transactions. An inter-

dealer market does not include a directory or listing of brokers, dealers, or traders for specific contracts (such as yellow sheets) that provides neither price quotations nor actual prices of recent transactions.

(ii) *Debt market.* A debt market exists with respect to a debt instrument if price quotations for the instrument are readily available from brokers, dealers, or traders. A debt market does not exist with respect to a debt instrument if—

(A) No other outstanding debt instrument of the issuer (or of any person who guarantees the debt instrument) is traded on an established financial market described in paragraph (b)(1)(i), (ii), (iii), (iv), (v), or (vi) of this section (other traded debt);

(B) The original stated principal amount of the issue that includes the debt instrument does not exceed \$25 million;

(C) The conditions and covenants relating to the issuer's performance with respect to the debt instrument are materially less restrictive than the conditions and covenants included in all of the issuer's other traded debt (e.g., the debt instrument is subject to an economically significant subordination provision whereas the issuer's other traded debt is senior); or

(D) The maturity date of the debt instrument is more than 3 years after the latest maturity date of the issuer's other traded debt.

(c) *Notional principal contracts.* For purposes of section 1092(d)—

(1) A notional principal contract (as defined in § 1.446-3(c)(1)) constitutes personal property of a type that is actively traded if contracts based on the same or substantially similar specified indices are purchased, sold, or entered into on an established financial market within the meaning of paragraph (b) of this section; and

(2) The rights and obligations of a party to a notional principal contract are rights and obligations with respect to personal property and constitute an interest in personal property.

(d) *Effective dates.* Paragraph (b)(1)(vii) of this section applies to positions entered into on or after October 14, 1993. Paragraph (c) of this section