

CHAPTER 2: STRUCTURE OF OPTIONS MARKETS

MULTIPLE CHOICE TEST QUESTIONS

1. Options are traded on which of the following exchanges?
 - a. NYSE Amex
 - b. NYSE Euronext (Arca)
 - c. Chicago Board Options Exchange
 - d. International Securities Exchange
 - e. all of the above
2. A call option priced at \$2 with a stock price of \$30 and an exercise price of \$35 allows the holder to buy the stock at
 - a. \$2
 - b. \$32
 - c. \$33
 - d. \$35
 - e. none of the above
3. A put option in which the stock price is \$60 and the exercise price is \$65 is said to be
 - a. in-the-money
 - b. out-of-the-money
 - c. at-the-money
 - d. exercisable
 - e. none of the above
4. Organized options markets are different from over-the-counter options markets for all of the following reasons except
 - a. exercise terms
 - b. physical trading floor
 - c. regulation
 - d. standardized contracts
 - e. credit risk
5. The number of options acquired when one contract is purchased on an exchange is
 - a. 1
 - b. 5
 - c. 100
 - d. 500
 - e. 8,000
6. The advantages of the over-the-counter options market include all of the following except
 - a. customized contracts
 - b. privately executed
 - c. freedom from government regulation
 - d. lower prices
 - e. none of the above

7. Which one of the following is not a type of transaction cost in options trading?
- the bid-ask spread
 - the commission
 - clearing fees
 - the cost of obtaining a quote
 - all of the above
8. If the market maker will buy at 4 and sell at 4.50, the bid-ask spread is
- 8.50
 - 4.25
 - 0.50
 - 4.00
 - none of the above
9. Which of the following is a legitimate type of option order on the exchange?
- purchase order
 - limit order
 - execution order
 - floor order
 - all of the above
10. The exercise price can be set at any desired level on each of the following types of options *except*
- FLEX options
 - equity options
 - over-the-counter options
 - all of the above
 - none of the above
11. An investor who owns a call option can close out the position by any of the following types of transactions *except*
- exercise
 - offset
 - expiring out-of-the-money
 - buying a put
 - none of the above
12. Which type of trader legitimately practices dual trading?
- floor brokers
 - off-floor option traders
 - board brokers
 - designated primary market makers
 - none of the above
13. The option price is also referred to as the
- strike
 - spread
 - premium
 - fee
 - none of the above

14. Index options trading on organized exchanges expire according to which of the following cycles?
- March, June, September, and December
 - each of the next four consecutive months
 - the current month, the next month, and the next two months in one of the other cycles
 - every other month for each of the next nine months
 - none of the above
15. An investor who exercises a call option on an index must
- accept the cash difference between the index and the exercise price
 - purchase all of the stocks in the index in their appropriate proportions from the writer
 - immediately buy a put option to offset the call option
 - immediately write another call option to offset
 - none of the above
16. Which of the following are long-term options?
- Bond options
 - LEAPS
 - currency options
 - Nikkei put warrants
 - none of the above
17. The exchange with the largest share of the options market is the
- American Stock Exchange
 - Boston Options Exchange
 - Chicago Board Options Exchange
 - Pacific Stock Exchange
 - Philadelphia Stock Exchange
18. A writer selected to exercise an option is said to be
- marginal
 - assigned
 - restricted
 - designated
 - none of the above
19. All of the following are forms of options *except*
- convertible bonds
 - callable bonds
 - warrants
 - mutual funds
 - none of the above
20. Which of the following index options is the most widely traded?
- S&P 500
 - Nikkei 225
 - Technology Index
 - New York Stock Exchange Index
 - none of the above

21. In which city did organized option markets originate?
- New York
 - Chicago
 - Philadelphia
 - San Francisco
 - none of the above
22. Who determines whether options on a company's stock will be listed?
- the clearing house
 - Securities Exchange Commission
 - the company
 - the exchange
 - none of the above
23. An order that specifies a maximum price to pay if buying is a
- stop order
 - market order
 - limit order
 - all or none order
 - none of the above
24. What amount must a call writer pay if a cash-settled index call is exercised?
- difference between the index level and the exercise price
 - exercise price
 - difference between the exercise price and the index level
 - index level
 - none of the above
25. Option traders incur which of the following types of costs?
- margin requirements
 - taxes
 - stock trading commissions
 - a and b
 - a, b and c
26. The total number of long option contracts outstanding at any given time is called the
- market cap
 - sum options outstanding (SOO)
 - option wealth outstanding (OWO)
 - open interest
 - none of the above
27. "Wal-Mart calls" are an example of
- an option series
 - an option class
 - an option grade
 - a and b
 - none of the above
28. This individual maintains and attempts to fill public option orders but does not disclose them to others.
- liquidity provider

- b. board broker
 - c. order book official
 - d. registered option trader
 - e. none of the above
29. What intermediary guarantees an option writer's performance?
- a. credit worthiness rating company
 - b. brokerage
 - c. good-till-canceled order
 - d. clearinghouse
 - e. none of the above
30. Suppose you hold a call option. The stock price has recently been increasing-making your call option more valuable. Through what process might you take advantage of the liquid nature of the options market?
- a. offsetting order
 - b. contract reconciliation
 - c. mark to market order
 - d. settling up
 - e. none of the above

CHAPTER 2: STRUCTURE OF OPTIONS MARKETS

TRUE/FALSE TEST QUESTIONS

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| T | F | 1. | The exercise price is also called the striking price. |
| T | F | 2. | The Put and Call Brokers and Dealers Association created the first organized options exchange. |
| T | F | 3. | An out-of-the-money call option has an exercise price less than the stock price. |
| T | F | 4. | A put option increases in value when the stock price decreases. |
| T | F | 5. | All of the options on Microsoft comprise an option class. |
| T | F | 6. | The AT&T October puts are an option series. |
| T | F | 7. | Exercise prices are set in \$5 increments for options on exchanges. |
| T | F | 8. | The over-the-counter options market is much larger than the exchange-listed options market. |
| T | F | 9. | Exchange-listed options expire on the Saturday following the third Friday of the month. |
| T | F | 10. | Position limits are restrictions on the number of transactions an investor can execute on a given day. |
| T | F | 11. | Exercise limits are restrictions on the number of options that can be exercised by an investor in a given day or series of days. |
| T | F | 12. | A market maker is an options trader who buys and sells options off of the exchange floor. |
| T | F | 13. | The bid price is the price paid to buy an option from a market maker. |
| T | F | 14. | Options traders who hold their positions for very short periods of time are called position traders. |
| T | F | 15. | An order placed by an investor for the broker to buy an option at the best available price is called a market order. |
| T | F | 16. | The number of option contracts outstanding at any given time is called the open interest. |
| T | F | 17. | Most investors close their positions by exercising their options. |
| T | F | 18. | Over-the-counter options are not subject to default. |
| T | F | 19. | Indices measuring options market activity are simple to construct and widely quoted. |
| T | F | 20. | The spread between the bid price and the ask price is a transaction cost to the option trader. |
| T | F | 21. | The options market is regulated by the Securities Investor Protection Corporation. |

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| T | F | 22. | Index options have less volume than stock options. |
| T | F | 23. | The Options Clearing Corporation guarantees the obligations of traders on options exchanges. |
| T | F | 24. | Offsetting an over-the-counter option contract cancels both contracts. |
| T | F | 25. | The order book official executes limit order option trades for the general public. |
| T | F | 26. | CBOE option market makers are also called liquidity providers. |
| T | F | 27. | Over-the-counter options dealers do not have to be members of an options exchange. |
| T | F | 28. | A market maker always avoids the cost of the bid-ask spread. |
| T | F | 29. | The majority of options exchanges in the U.S. are fully automated. |
| T | F | 30. | Option commissions are set by the Chicago Board Options Exchange. |
| T | F | 31. | On the CBOE, option tables represent each option with a series of letters and number, such as, MSFT\12B17\20.0. The last number represents the calendar date, the 20 th of the month in this example. |
| T | F | 32. | Again, on the CBOE, option tables represent each option with a series of letters and number, such as, MSFT\12B17\20.0. The middle letter represents the calendar month and whether it is a call or put. |
| T | F | 33. | An investor who is long an over-the-counter call option is exposed to the risk that the call writer will default on her obligations should the call option end up in-the-money. |
| T | F | 34. | Exercising a stock put option means the put seller must sell stock at the stated strike price. |
| T | F | 35. | A call option to buy euros expressed in \$/€ is equivalent to a put option to sell dollars expressed in €/ \$. |