TAXES & INVESTING

A Guide for the Individual Investor

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This booklet provides a summary of certain U.S. federal income tax rules affecting investments in various financial instruments, including stocks, bonds, options and futures contracts. This summary is for general information purposes only and is not intended to address any individual investment or tax situation. Various rules and exceptions may apply to your particular circumstances that are not specifically covered in this booklet, and material contained in this booklet may be affected by changes in law subsequent to publication. You should seek advice based on your particular circumstances from an independent tax advisor.

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Introduction and Highlights of Recent Changes

This booklet summarizes the basic rules governing the federal income taxation of certain financial investments by individuals who are citizens or residents of the United States and who dispose of an investment in a taxable transaction. It does not attempt to describe all the rules that may apply to a particular transaction and is not a treatise on the taxation of financial instruments. Examples have been provided to illustrate the application of various rules. Generally, the effect of commissions has not been taken into account. Corporations, tax-exempt institutions, mutual funds and various other market participants may be subject to different rules than those described in this booklet.

There have been several important changes in the tax law since this booklet was last updated in 2011. These changes include an increase in the maximum income tax rates on capital gains and qualified dividends from 15% to 20% for persons in the highest tax bracket (now 39.6%).

The following chart summarizes the maximum tax rates currently in effect for upper-income individual investors. For 2015, the higher rate applies to taxpayers with taxable income over $413,200 (for single filers) or $464,850 (married filing jointly). There is also a new tax of 3.8% on net investment income (the "NII Tax") which applies to taxpayers with adjusted gross income over $200,000 (single filers) or $250,000 (married filing jointly). The threshold amounts for the NII Tax are not indexed for inflation.

Top Combined Federal Tax Rates
(Regular Income Tax Plus 3.8% Tax
on Net Investment Income)

Long-term Capital Gains	23.8%
Short-term Capital Gains	43.4%
60/40 Gains	31.64%
Interest	43.4%
Qualified Dividends	23.8%

This edition of *Taxes & Investing: A Guide for the Individual Investor* reflects changes in the federal income tax law through December 2014. Because the tax law changes frequently, it is very important to check with a tax advisor about possible changes or clarifications in the law.

Dividends

Dividends received by an individual shareholder from domestic corporations and "qualified foreign corporations" are generally taxed at the same rates that apply to net capital gain for purposes of both the regular tax and the alternative minimum tax. See discussion on page 7. Thus, qualifying dividends are currently taxed at a top rate of 20% (plus the 3.8% tax on net investment income).

Dividends paid by a foreign corporation with respect to stock that is "readily tradable on an established securities market in the United States" are generally eligible for these lower rates. Under guidance issued by the Internal Revenue Service, common or ordinary stock, preferred stock, or an American depositary receipt in respect of such stock, is considered "readily tradable on an established securities market in the United States" if it is listed on a national securities exchange. Registered national securities exchanges include BATS Exchange, Inc., C2 Options Exchange, Incorporated, Chicago Board Options Exchange Incorporated, Chicago Stock Exchange, Inc., EDGA Exchange, Inc., EDGX Exchange, Inc., International Securities Exchange, LLC, NASDAQ OMX BX, Inc., NASDAQ OMX PHLX, Inc., The NASDAQ Stock Market LLC, National Stock Exchange, New York Stock Exchange LLC, NYSE Arca, Inc., and NYSE Amex LLC.

For these lower tax rates to apply, an investor must hold the stock for at least 61 days during the 121-day period beginning 60 days before the ex-dividend date for a particular dividend payment (at least 91 days during the 181-day period beginning 90 days before the ex-dividend date in the case of certain preferred stock). The holding period must be satisfied for each dividend payment. Days on which the stock position is hedged, other than with at-the-money or out-of-the-money "qualified covered calls" (described on pages 19-22), generally do not count for purposes of the holding period requirement. In determining the holding period, the day on which stock is disposed of is taken into account, but not the day on which it is acquired.

Example:
On July 7, 2014, an investor buys 100 shares of XYZ Co. common stock for $53. On July 22, 2014, the investor buys an XYZ/October/55 put. On August 13, 2014, the investor sells the put. On August 19, XYZ Co. stock goes ex-dividend with respect to a distribution to shareholders of record on August 22, 2014. On October 15, 2014, the investor sells the XYZ Co. stock. The investor is entitled to the lower tax rate on the dividend paid because the XYZ Co. stock is held for a total of at least 61 days during the 121-day period beginning 60 days before August 19, the ex-dividend date. Days on which the investor held the XYZ/October/55 put are not taken into account.

Example:
On September 9, 2014, an investor buys 100 shares of XYZ Co. common stock for $38. On October 13, 2014, the investor writes an XYZ/December/40 call. The closing price of XYZ Co. stock on the previous day was $41. The option is an in-the-money qualified covered call. On November 14, 2014 the investor closes out the XYZ/December/40 call by making a closing purchase. On November 16, 2014 the XYZ Co. stock goes ex-dividend with respect to a distribution to shareholders of record on November 19, 2014. The investor sells the XYZ Co. stock on December 2, 2014. The investor is not entitled to the lower tax rate on the dividend paid because the XYZ Co. stock is not held for at least 61 days during the 121-day period beginning 60 days before November 16, 2014, the ex-dividend date. Days on which the short XYZ/December/40 call is outstanding are not taken into account.

The lower tax rate is not available for dividends received to the extent that the taxpayer is obligated to make related payments with respect to positions in substantially similar or related property (e.g., "payments in lieu of dividends" on shares borrowed for use in a short sale). Similarly, owners whose shares are lent pursuant to a securities lending agreement on the record date for a dividend are not entitled to the lower rate on amounts received in respect of the shares lent, i.e., the lower rate does not apply to payments in lieu of dividends. Dividends eligible for the reduced rate are not treated as "investment income" for purposes of determining the limitation on deductibility of investment interest expense (see page 38) unless the investor elects to treat the dividends as not eligible for the lower tax rate.

Capital Gains and Losses

Short-term capital gains (gains from capital assets held for one year or less) are subject to tax at ordinary rates, currently up to 39.6%, plus the NII tax of 3.8% for upper income taxpayers (see pages 3-4).

A "maximum" tax rate of 20% applies to most long-term capital gains (i.e., gains from assets with a holding period of more than one year). The 20% rate generally applies to long-term capital gains from investments in stock and securities, but there are exceptions. Higher rates apply to certain other long-term capital gains (e.g., collectibles gain, which includes gains from gold and other precious metals, is taxed at 28%). The 3.8% NII tax applies on top of these rates.

With a 19.6% percentage point spread between the 20% long-term and 39.6% short-term capital gain tax rates, individual investors with profitable positions may in some cases have an incentive to hold such positions for at least a year and a day to get the benefit of the lower rate. However, days on which a position is hedged (e.g., by a purchased put option) generally do not count for holding period purposes and can actually result in forfeiting existing holding periods. See discussion of tax straddles on page 17.

In evaluating investment decisions, investors should take into account any effect of the individual alternative minimum tax ("AMT"). In general, the

AMT is imposed on a graduated two-tier basis, 26% and 28%, based on the amount of alternative minimum taxable income. However, the tax law conforms the capital gains tax rate a taxpayer would pay under the regular tax with the rate for AMT purposes through an AMT capital gains tax rate. This rate equals the capital gains tax rate under the regular tax, according to the type of asset and the length of holding period. Accordingly, capital gains and dividend income taxed at capital gains rates alone should not affect whether a taxpayer becomes subject to the AMT.

Losses are subject to certain limitations. Capital losses (long-term as well as short-term) are allowed in full to the extent of capital gains plus $3,000 of ordinary income. Special netting rules apply to take into account the multiple rates for long-term capital gains. The ability to reduce ordinary income by up to $3,000 of capital losses does not apply for purposes of the NII Tax.

The use of the installment method of reporting for sales of publicly traded property is not permitted. Individuals are required to recognize gain or loss on the sale of publicly traded stock and securities on the day the trade is executed.

When an individual investor sells stock acquired in 2011 or later years,, brokers are generally required to report to the Internal Revenue Service the tax basis of the stock sold. This information will also be provided to the investor on the same form (IRS Form 1099-B) that is used to report the proceeds from a sale of stock. Brokers are also required to report whether gain or loss from the sale of stock is long-term or short-term. Brokers are required to report this basis and holding period information for stock acquired after December 31, 2010, and are permitted to report such information for stock acquired at an earlier time. Unless an investor otherwise instructs the broker, the broker will generally report shares sold on a first-in, first-out basis. In other words, the earliest acquired shares in an account are treated as sold first. Similar reporting requirements apply to mutual fund shares and shares in a dividend reinvestment plan acquired after 2011 as well as to options entered into and most debt instruments acquired, after 2013.

Wash Sale Rule

The wash sale rule prevents taxpayers from selling stock or securities (including options) at a loss and reacquiring "substantially identical" stock or securities (or options to acquire substantially identical stock or securities) within the 30-day period before the sale occurs or the 30-day period after the sale occurs. The wash sale rule also prevents taxpayers from currently recognizing losses on the closing of short sales if, within 30 days before or 30 days after the closing, substantially identical stock or securities are sold or the taxpayer enters into another short sale of substantially identical stock or securities. The meaning of the term "substantially identical" is generally the same as in the case of the short sale rules, as discussed on page 10.

When the wash sale rule applies, the loss is disallowed and the basis of the replacement property is deemed to be the basis of the original property, increased or decreased, as the case may be, by the difference between the cost of the replacement property and the price at which the old property was sold. The holding period of the original property is added to the holding period of the newly acquired replacement property.

The Internal Revenue Service has taken the position that the wash sale rule will disallow a loss on the sale of stock if, within 30 days before or after the sale of the stock, the taxpayer sells an "in-the-money" put option with respect to the stock and, on the basis of objective factors at the time the put was sold, there is a substantial likelihood that the put will be exercised. These factors include the spread at the time the put is sold between the value of the underlying stock and the exercise price of the put, the premium paid and the historic volatility in the value of the stock.

The IRS also takes the position that the wash sale rule will apply if a taxpayer sells stock or securities at a loss and within 30 days before or after the sale substantially identical stock or securities are purchased in an Individual Retirement Account ("IRA") owned by the taxpayer. The IRS has further ruled that in this situation, the investor's basis in the IRA is not increased to reflect the disallowed loss.

Example:
An investor holds 100 shares of XYZ Co. stock with a basis of $70 a share. On December 15, 2014, the investor sells the 100 shares for $20 a share, incurring a loss of $50 a share. On January 10, 2015, the investor purchases 100 shares of XYZ stock for $25 per share. The loss on the sale of shares in December 2014 is disallowed under the wash sale rule. The investor has a basis in the new shares of $75 a share.

Example:
On January 6, 2014, an investor sells short 100 shares of XYZ Co. for $50 per share. On April 5, 2014, the investor purchases 100 shares of XYZ Co. at $55 per share and delivers the stock to close the short position, resulting in a $500 loss. On April 28, 2014, the investor sells short 100 shares of XYZ Co. for $52 per share. The $500 loss on the closing of the first short sale is disallowed because the investor, within 30 days after closing the short sale at a loss, entered into another short sale of substantially identical stock.

Short Sales and Constructive Sales

Short Sales

The short sale rules deal with the selling of stock or securities in a short sale when the taxpayer holds or subsequently acquires "substantially identical property." Under the short sale rules, if the investor has held the stock or securities for one year or less at the time of the short sale, or if substantially identical property is acquired while the short sale remains open, gain on closing the short sale is a short-term capital gain (notwithstanding the period of time any property used to close the short sale has been held). In addition, the holding period of the long position (in the order of the dates of acquisition but only to the extent of the quantity sold short) is forfeited, i.e., it reverts to zero. The holding period of the long position begins to run again only after the short sale has been closed. If the long position has already been held more than 12 months at the time of the short sale, no termination of its holding period occurs, but any loss on closing the short sale is a long-term capital loss. A taxpayer can deliver against the short position, for long-term capital gain, stock held more than 12 months at the time of the short sale, provided that no other substantially identical property was held short-term at the time of the short sale or acquired while the short sale was open.

Acquiring an option to sell (a "put") is treated as a short sale for purposes of the short sale rules, but a "married put" has been exempted from these rules. However, a married put appears to be subject to the tax straddle rules, discussed on page 17.

The "substantially identical" test generally requires that the securities be of the same issuer and be commercially identical in all major respects, including interest rate, maturity date, dividend provisions, liquidation preferences and other similar terms. Thus, stocks of two different issuers are generally not substantially identical even if the issuers are in the same industry. Although a short sale of the stock of one issuer while holding stock of the second issuer may not constitute a short sale, the positions may be subject to the tax straddle rules if they are "substantially similar or related." See discussion on page 17.

Constructive Sales

As a result of the "constructive sale" rule and subject to various exceptions, a taxpayer must recognize gain (but not loss) upon entering into certain transactions that effectively eliminate substantially all of the taxpayer's risk of loss and upside gain potential with regard to any appreciated position with respect to stock, a partnership interest or certain debt instruments. Entering into short sales, futures or forward contracts, and total return equity swaps are examples of transactions that may result in constructive sales. Where a short position in stock has appreciated, the acquisition of the stock may also result in a constructive sale. Other transactions to be covered by these rules may be identified in Treasury regulations, which may apply retroactively to prevent abuse.

When a constructive sale occurs, gain is recognized as if the position were sold at its fair market value and immediately repurchased. The basis of the appreciated position is increased by any gain realized, and a new holding period begins as if the position had been acquired on the date of the constructive sale.

The constructive sale rule does not apply to transactions that meet three conditions: (1) the transaction is closed before the end of the 30th day after the close of the taxable year in which it was entered into; (2) the appreciated position is held throughout the 60-day period beginning on the date such transaction is closed; and (3) during such 60-day period, the taxpayer does not enter into transactions that would diminish the risk of loss on such position. At-the-money and out-of-the-money qualified covered calls are not treated as risk-reducing transactions for this purpose. A special rule applies where one or more risk–reducing transactions are entered into within such 60-day period and are also closed before the 30th day after the end of the year in which the initial transaction occurred. The constructive sale rule will not apply if all such risk-reducing transactions are closed before the 30th day after the end of the taxable year in which the would-be constructive sale transaction was entered into and the appreciated position is held unhedged thereafter for 60 days.

A transaction that results in a constructive sale of one appreciated position is not treated as resulting in the constructive sale of any other appreciated position so long as the taxpayer continues to hold the position that was treated as constructively sold. However, when that position is sold or otherwise disposed of, the constructive sale transaction (if it remains open) can cause a constructive sale of another appreciated position.

If less than all of a position is constructively sold, the taxpayer may specifically identify the specific tax lots that have been "sold." Absent that identification, the position is deemed to be sold in the order acquired (i.e., on a "first in, first out" basis).

There are as yet no specific rules that determine whether entering into one or more options positions constitutes a constructive sale. The legislative history of the constructive sale provision makes clear, however, that Treasury regulations are expected to treat options transactions that eliminate substantially all risk of loss and opportunity for gain as constructive sales. These regulations are not to apply retroactively except to prevent abuse.

Transactions discussed in this booklet involving options do not reflect the potential application of the constructive sale rule in advance of regulatory guidance.

Example:
On June 3, 2014, an investor buys 100 shares of X Co. stock for $50 per share. On August 18, 2014, the investor sells short 100 shares of X Co. for $60 per share. On January 6, 2015, the investor closes the short position by delivering the 100 shares purchased on June 3, 2014. Entering the short sale on August 18 is a constructive sale, resulting in a $1,000 gain in 2014. Since the 100 shares bought on June 3, 2014 are treated as sold and repurchased for $60 upon entering the short sale, no further gain or loss is realized on closing the short sale in 2015.

Example:
Using the prior example, assume that the investor acquires 100 shares of X Co. stock "in the market"

on January 6, 2015 for $65 per share and delivers those shares to cover the short position instead of delivering the shares purchased on June 3, 2014. The investor holds the shares of X Co. acquired on June 3, 2014 for 60 days after closing out the short position without hedging that position. There is no constructive sale of X Co. stock in 2014, and the investor realizes a $5 per share loss on closing out the short position in January 2015.

Example:
On May 4, 2014, an investor buys 100 shares of Y Co. stock for $25 per share. On July 12, 2014, the investor sells 100 shares of Y Co. short for $20 per share. There is no constructive sale on July 12 because the investor's Y Co. shares were not appreciated at the time of the short sale.

Example:
On February 3, 2014, an investor buys 200 shares of Z Corp. stock at $30 per share. On April 22, 2014, the investor buys at-the-money puts (exercise price equals current market price of the underlying stock) on the 200 shares when the stock is $40 per share. The acquisition of the at-the-money puts does not trigger the constructive sale rule because the options reduce only the investor's risk of loss. However, the tax straddle rules will apply. See page 17.

Example:
On January 7, 2014 an investor directs a broker to borrow 100 shares of XYZ Co. stock and to sell it short. The investor does not own any XYZ Co. stock. On December 30, 2014, when the stock's value has decreased and the value of the investor's short position has increased, the investor purchases 100 shares of XYZ Co. stock and those shares are delivered to the lender of the stock to close the short sale on January 3, 2015. Under the constructive sale rule, since the short position has appreciated at the time of the purchase of the stock, the investor realizes the gain on December 30, 2014. Conversely, if at the time of the stock purchase, the value of the investor's short position

has decreased (the stock price has increased since January 7, 2014), the loss on closing the short sale is not realized until the stock is delivered on January 3, 2015.

One-Sided Equity Option Positions

The treatment of gain or loss as long-term or short-term may have great significance for equity options because of the preferential rate for long-term capital gain. Except as otherwise indicated, the discussion in this section assumes that the tax straddle rules (discussed on pages 17-26) do not apply to alter the results under the general rules. The discussion below does not apply to options that are "Section 1256 contracts" (discussed on pages 26-27).

Long Calls

If a call option is acquired and held for more than one year, the resulting gain or loss on the sale is a long-term capital gain or loss (see page 7). If the call is purchased and sold in one year or less, any resulting gain or loss is short-term. Expiration of a call is treated as a sale or exchange on the expiration date and results in a short-term or long-term capital loss, depending on the holding period of the call. If the call is exercised, the premium paid, the strike price, the brokerage commission paid upon exercise, and the commission on the call's purchase are all included in the basis of the stock. The holding period of the stock acquired begins on the day after the call is exercised and does not include the holding period of the call.

Short Calls

Premium received for writing a call is not included in income at the time of receipt, but is held in suspense until the call expires or the writer either sells the underlying stock as a result of the assignment of the call or closes out the option by entering into a closing transaction. If the call expires, the premium is taken into income as short-term capital gain regardless of the length of time the call is outstanding.

Similarly, gain or loss on the termination of the option through a closing transaction is short-term capital gain or loss, regardless of the length of time the call is outstanding. However, if a call is assigned, the strike price plus the premium received becomes the sale price of the stock in determining gain or loss. The tax treatment of the resulting gain or loss depends upon the holding period and the basis of the underlying property used to make the delivery to satisfy the assignment. If the stock delivered has a holding period greater than one year (taking into account the tax straddle rules), the gain or loss would be long-term.

Long Puts

If an investor purchases a put option, any gain or loss on the termination of the put (through a closing transaction or expiration) is short-term or long-term capital gain or loss, depending on the holding period of the put. The expiration of a long put results either in a short-term capital loss if the put is held one year or less or in a long-term capital loss if held for more than one year. If the put is exercised, the cost of the put and the commission on the sale of the stock reduce the amount realized upon the sale of the underlying stock delivered.

Short Puts

As with call premium, put premium is held in suspense until the put writer's obligation is terminated. Closing out a short put results in short-term capital gain or loss regardless of the length of time the put is outstanding. If the put expires, the writer realizes a short-term capital gain to the extent of the premium received. If the put is assigned, the strike price plus commission less the premium received for writing the put becomes the basis of the stock acquired, and the holding period begins for the stock on the day after the stock's purchase.

Treatment of Gain or Loss on Disposition of One-Sided Equity Options (If Not Exercised)

Time Option Position Held	Long Call	Short Call	Long Put	Short Put
Less than or equal to 1 year	Short-term	Short-term	Short-term	Short-term
Greater than 1 year	Long-term	Short-term	Long-term	Short-term

Offsetting Positions: The Tax Straddle Rules

The tax straddle rules are extremely complex. While they are intended to prevent taxpayers from deducting losses before offsetting gains have been recognized, the rules are very mechanical and can apply in unexpected contexts to disallow loss deductions and to cause other adverse tax effects.

Generally, a straddle for Federal income tax purposes involves the holding of "offsetting positions" with respect to actively traded personal property (such as stocks, bonds, commodities and currencies). Positions are considered to be offsetting if any position held substantially diminishes the risk of loss associated with holding one or more other positions. If one position substantially diminishes the risk of loss on another position, it would appear that the tax straddle rules apply even if the second position does not reduce risk of loss associated with the first position. In other words, risk diminution does not appear to require mutuality.

Once an investor holds two positions that meet the "substantial diminution of risk of loss" test, the consequences include the following:

1. No current deduction for losses is allowable to the extent of the unrecognized gain (if any) at the end of the taxable year in positions that were offsetting to the loss position. Deferred losses are treated as sustained in the next taxable year, when

they are again subject to deferral to the extent of any offsetting unrecognized gain at the end of such year. However, see discussion of "Identified Straddles" on page 25.

The deferral of losses applies only to the extent of unrecognized gain in offsetting positions. If the loss exceeds the unrecognized gain in such positions at year-end, the excess loss is not deferred.

Loss deferral is also required to the extent of any unrecognized gain at year-end in a "successor position" or "positions that are offsetting to a successor position." In general, a "successor position" is a position which is on the same side of the market (long or short) as was the original loss position, which replaces a loss position and which is entered into during a period commencing 30 days prior to and ending 30 days after the disposition of the loss position. However, a position entered into after all positions of a straddle have been disposed of will not be considered a successor position.

2. If a position that has been held for one year or less becomes part of a straddle, the holding period in the position is forfeited (see Appendix II). The holding period for such a position begins again (at zero) when the position is no longer part of a straddle.

3. If a taxpayer holds a position that, if sold, would give rise to long-term capital gain or loss and enters into an offsetting position, any loss on the disposition of that offsetting position will be treated as long-term rather than short-term.

4. All carrying charges and interest expense (including margin) incurred during the period of offset are required to be capitalized and added to the basis of the position to which they are allocable. Such capitalized charges are, however, reduced by income generated by positions in the straddle such as divi-

dends received on stock included in the straddle. Because the (net) cost of carrying the positions in the straddle is capitalized into basis, it will decrease the potential capital gain or increase the potential capital loss upon disposition.

As a result of legislation in 2004, long stock and a short sale of that stock (a "short against the box") are now treated as offsetting positions for purposes of the tax straddle rules. Previously, a taxpayer holding stock and entering into a short sale of the stock was subject to the short sale rules (described on page 10) but not to the tax straddle rules. Now both the short sale rules and the tax straddle rules can apply.

The substantial diminution of risk of loss test does not require that offsetting positions be of the same issuer. In the case of stock, an offsetting position (such as a put option) must relate to "substantially similar or related property." As a result, it is possible, depending on the circumstances, that stock of one issuer and options on the stock of another issuer may be viewed as offsetting positions. In contrast, as explained above, the concept of "substantially identical" stock for purposes of the wash sale and short sale rules generally requires that the stock involved be stock of the same issuer.

Qualified Covered Calls

The tax straddle rules described above do not apply to combinations of positions that consist of stock and "qualified covered calls" with respect to the stock. This exception is not available however, if these positions are part of a larger combination of positions that constitute a tax straddle.

A "qualified covered call" is a call option written on stock held by the investor (or stock acquired by the investor "in connection with" the writing of the option). In order to qualify, the call option must generally be traded on an exchange, though certain over-the-counter options also qualify.

The call option must have more than 30 days to expiration at the time it is written and a strike price that is not "deep-in-the-money." Subject to various special rules (described below), an option is deep-in-the-money for this purpose if the strike price is less than the first available strike price below the closing price of the stock on the day before the option was written. It is important to know the strike price intervals that are available since different strike price intervals (e.g., $0.50, $1, $2.50 or $5) may exist among the various listed options for comparably priced stocks. Special rules, discussed below, apply to long-dated calls and calls on stocks priced at or below $25.

For an option written with more than 90 days to expiration and with a strike price over $50, the call must have a strike price no lower than the second available strike price below the closing stock price on the previous day. If the stock price is $150 or less, however, a qualified covered call cannot be more than $10 "in-the-money." In other words, the strike price cannot be more than $10 below the closing price of the stock on the previous day. Under another special rule, if the closing price of a stock on the previous day is $25 or less, the strike price must be at least 85% of that stock price. As a result, even the first strike price below the previous day's closing price will be "deep-in-the-money" unless that strike price is at least 85% of the prior day's closing price. The U.S. options exchanges trade options with $0.50 strike price intervals on a limited number of very low-priced stocks. For a table of in-the-money qualified covered calls for stock priced $25 or less, see Appendix I.

In all cases, if the opening price of the stock on the day the option is written is greater than 110% of the preceding day's closing price, that opening price is substituted for the preceding day's closing price in applying the rules described above to determine the lowest acceptable strike price for a qualified covered call. The following chart may help covered call writers determine which options are qualified covered calls:

Qualified Covered Calls

Previous Day's Closing Stock Price*	Lowest Acceptable Strike Price**
$25 or less More than 30 days to expiration	One strike below previous day's closing stock price (no in-the-money qualified covered call if strike price is less than 85% of stock price)
$25.01 to $50 More than 30 days to expiration	One strike below previous day's closing stock price
$50.01 to $150 31-90 days to expiration	One strike below previous day's closing stock price
$50.01 to $150 More than 90 days to expiration	Two strikes below previous day's closing stock price as long as strike price is greater than $50 (but not more than $10 in-the-money)
Greater than $150 31-90 days to expiration	One strike below previous day's closing stock price
Greater than $150 More than 90 days to expiration	Two strikes below previous day's closing stock price

* If the opening price on the day the option is written exceeds the previous day's closing price by more than 10%, then that opening price is used in determining the lowest acceptable strike price.
** Whether a covered call is "qualified" is subject to certain special rules, described below.

See page 24 for additional requirements that apply to options with terms greater than 12 months.

Example:
An investor purchases shares of XYZ Co. stock at $61 per share on September 3, 2014 and writes a covered call on the same day. XYZ Co. closed at $61

per share on September 2, 2014. A call with a strike price of $60 is the only 31-90 day in-the-money qualified covered call that can be written. A $55 or $60 strike price call can be written if the call has more than 90 days to expiration, assuming $5 strike price intervals. If $2.50 strike price intervals exist for XYZ Co., a $57.50 or $60 strike price qualified covered call can be written.

Example:
Assume, instead, that the investor purchases shares of XYZ Co. stock at $114 per share, which was also the previous day's closing price. A call with a strike price of $110 is the only 31-90 day in-the-money qualified covered call that can be written (assuming $5 strike price intervals). An in-the-money qualified covered call with more than 90 days to expiration may be written at $105 or $110 (again, assuming $5 strike price intervals).

Example:
If XYZ Co. shares closed at $11.80 per share on the previous day, no in-the-money qualified call is available, assuming $2.50 option strike intervals (see Appendix I), since the strike price must be at least 85% of the stock price (the $10 strike price options are less than 85% of $11.80). However, if $1 strike price intervals exist, an $11 strike price qualified covered call can be written.

Even if the stock price/strike rules are satisfied, a call is not qualified unless it is an option to purchase stock owned by the investor at the time the option is written or acquired by the investor "in connection with" the granting of the option. For example, a call written on October 12, 2014 will not be qualified if the stock is purchased on October 18, 2014.

Covered Calls - Special Rules

Writing an at-the-money (strike price of call equals the stock price used in determining the lowest acceptable strike) or an out-of-the-money (above-the-market) qualified covered call allows the holding period of the underlying stock to continue. However, an in-the-money qualified covered call suspends the holding period of the stock during the time of the option's existence. Further, any loss with respect to an in-the-money qualified covered call is treated as long-term capital loss, if at the time the loss is realized, gain on the sale or exchange of the underlying stock would be treated as long-term capital gain.

Additionally, when a covered call is disposed of at a loss in one year and the stock is sold for a gain in the subsequent year, the stock must be held at least 30 days from the date of disposition of the call in order to avoid application of the loss deferral rule described on pages 17-18. Generally, only days on which the stock is held "naked" may be counted in determining whether the 30-day holding period is satisfied. However, the holding period continues to run while the taxpayer is the writer of at-the-money or out-of-the-money (but not in-the-money) qualified covered calls. Similarly, if the underlying stock is sold at a loss in one year and a gain from the call option is included in the following year, the loss deferral rule will apply if the call is not held for at least 30 days after the stock was sold.

Example:

On December 1, 2014 an investor purchases 100 shares of XYZ Co. stock at $36 per share. On the same day, the investor writes an XYZ/February/35 call, receiving a premium of $3. On December 15, 2014 the investor unwinds his position in the XYZ/February/35 call by making a closing purchase at $5. On May 1, 2015, the investor sells the 100 shares of XYZ Co. stock at $45 per share. No positions, long or short, in XYZ Co. stock or options are established by the investor after the option closing purchase on December 15, 2014 and prior to the sale of the stock on May 1, 2015. The loss on the covered call is not subject to the loss deferral rule because the XYZ Co. stock is held for 30 days or more after the close of the call.

Example:

On November 6, 2014, an investor purchases 100 shares of XYZ Co. stock at $42. On the same day, the investor writes an XYZ/February/40 call receiving a premium of $4. On December 27, 2014, the investor unwinds his position in the XYZ/February/40 call by making a closing purchase of $6. On January 6, 2015, the investor sells the XYZ Co. stock for $46. The covered call is subject to the loss deferral rule, because the XYZ Co. stock was not held for 30 days after the close of the call at a loss in the year preceding the sale of the stock at a gain. The loss on the call is deferred until 2015 to the extent of the unrecognized gain in the XYZ Co. stock on December 31, 2014.

Special Rules for Long-Dated Call Options

- Covered calls with a term exceeding 33 months are not eligible to be treated as "qualified covered calls."
- For options with a term greater than 12 months (but not exceeding 33 months), the closing stock price on the previous day (or the opening price on the day the option is written when that opening price exceeds the prior day's closing price by more than 10%) is adjusted by a factor as set forth in the chart below in determining whether the strike price of the option meets the requirements for a qualified covered call.

Option Term		Adjustment Factor
Greater Than	Not More Than	
12 months	15 months	1.08
15 months	18 months	1.10
18 months	21 months	1.12
21 months	24 months	1.14
24 months	27 months	1.16
27 months	30 months	1.18

Example:

An investor owns XYZ Co. stock and on July 16, 2014 writes a 21-month call option on the stock.

XYZ Co. closed at $100 per share on July 15, 2014. The adjustment factor for a 21-month option is 1.12, and the "adjusted" stock price is therefore $112. Accordingly, if $5 strike price intervals exist for XYZ Co. options, the lowest eligible stock price for a qualified covered call is $105.

Identified Straddles

As a result of the 2004 Act, investors may avoid some of the harsh effects of the loss deferral rule by identifying offsetting positions that are components of a straddle (an "identified straddle"). The identification must be made by the close of the day on which the investor enters into a transaction that creates the straddle. If there is a realized loss with respect to a position that is part of an identified straddle, the normal loss deferral rule (see pages 17-18) does not apply to that loss. Instead, the basis of each of the identified positions that offset the loss position is increased by an allocable portion of the loss. As a result, the investor will get the benefit of the loss as such offsetting positions are sold. Positions that are part of an identified straddle will not be treated as offsetting to positions that are not part of the identified straddle.

Physical Settlement Rule

The physical settlement of a straddle position (e.g., an options contract) established after October 21, 2004, that if terminated would result in a realization of a loss, is treated as a two-step transaction for purposes of applying the tax straddle rules. First, the position is treated as having been terminated for its fair market value immediately before the settlement. Then, the property (e.g., stock) used to physically settle the position is treated as having been sold at fair market value.

Mixed Straddles

When a straddle consists of one or more Section 1256 contracts (see below) and one or more positions that are not Section 1256 contracts, a "mixed straddle" results. The taxation of mixed straddles is exceedingly complex and is dependent, in part, on whether certain elections are made, and whether net gain or loss is attributable to the Section 1256 contracts or to the non-Section 1256 positions. Loss deferral and capitalization rules also apply (see pages 17-19).

Non-Equity and Stock Index Instruments

Certain exchange-traded options, and most futures contracts, are subject to special tax rules. These options and futures, which are known as "Section 1256 contracts," are treated as sold ("marked to market") on the last day of the year. Gain or loss resulting from such marking to market (or from an actual disposition) is treated as 60% long-term capital gain or loss and 40% short-term capital gain or loss ("60/40 treatment") regardless of how long the contract has been held. Any subsequent gain or loss is adjusted to reflect mark-to-market gains and losses previously taken into account.

This mark-to-market, 60/40 treatment applies to exchange-traded options on broad-based stock indexes (such as the S&P 500 index). It also applies to exchange-traded options on underlying property that is not equity based ("non-equity options"), such as interest-rate options and options on foreign currencies.

Foreign equity index warrants traded on U.S. exchanges are subject to the same tax considerations as options. Thus, foreign equity index warrants with respect to broad-based stock indexes generally should be treated as Section 1256 contracts.

Options on a stock index that is "narrow based" are subject to the rules governing the taxation of equity options and are not subject to 60/40, mark-to-market treatment. An index is narrow based if (1) it contains nine or fewer component securities, (2) a single component security comprises more than 30% of the index's weighting or (3) the five highest-weighted component securities in the aggregate comprise more than 60% of the index weighting.

As a result of the Dodd-Frank legislation enacted in 2010, various types of "swaps" are excluded from the definition of Section 1256 contracts and thus do not receive 60/40, mark-to-market treatment even if traded on an exchange. These swaps – which include interest rate swaps, equity swaps, credit default swaps, and similar instruments – have not traditionally been available for trading on securities exchanges or commodities exchanges. However, exchange-trading of such instruments has begun in recent years and the Dodd-Frank legislation is expected to increase this trend. The precise scope of the "swaps" exclusion from 60/40, mark-to-market treatment is unclear and guidance from the IRS is needed.

Except as discussed below, futures contracts (and options on futures contracts) traded on U.S. exchanges are generally subject to mark-to-market, 60/40 treatment.

Futures Contracts on Individual Stocks and Narrow-Based Stock Indexes

As a result of legislation enacted in 2000, trading in futures contracts on individual stocks and narrow-based stock indexes (as well as options on these futures) is now permitted. These futures are referred to as "securities futures contracts." Trading in such instruments began in November, 2002.

For investors, securities futures contracts are taxed in a manner similar to equity options rather than like most types of futures contracts. Accordingly, they are not subject to mark-to-market, 60/40 treatment. Gains and losses from securities futures contracts are treated as capital gains or losses. Gain or loss on the sale of a "long" securities futures contract will be long-term capital gain or loss if the contract is held more than one year, and short-term capital gain or loss if the contract is held for one year or less. Gain or loss on the sale of a "short" securities futures contract will be short-term regardless of how long the investor has held the contract (except as provided under the tax straddle rules). The holding period for securities acquired pursuant to a long securities futures contract includes the investor's holding period for the contract.

Entering into securities futures contracts can trigger the wash sale, short sale, tax straddle and constructive sale rules. For example, an investor who sells stock at a loss and enters into a long securities futures contract to purchase the same stock within 30 days before or after the sale is subject to the wash sale rule. Similarly, an investor who holds an appreciated stock position and enters into a short securities futures contract with respect to the same stock will have a constructive sale event unless three conditions (as set forth in the constructive sale provisions) are met: (1) the securities futures contract is unwound before the end of the 30th day after the close of the taxable year; (2) the stock position is held throughout the 60-day period beginning on the date the short securities futures contract is unwound; and (3) during the 60-day period, the stock position remains unhedged.

Exchange-Traded Funds

Exchange-traded funds (ETFs) are generally open-end investment companies that hold securities constituting or based on an index or portfolio of securities. Examples of such funds are Standard & Poor's Depositary Receipts ("SPDRs"), NASDAQ-100 Index Tracking Stock (the "QQQ") and DIAMONDS. Investments in ETFs are generally taxed in the same way as investments in a mutual fund (a "regulated investment company" for Federal income tax purposes). Thus, dividends paid from investment income (including dividends, interest and net short-term capital gains) are generally taxable to beneficial owners as ordinary income. Dividends attributable to qualifying dividends earned by the fund may qualify for the reduced rate under present law (see page 5). Similarly, capital gain distributions from net long-term capital gains of the fund are taxable as long-term capital gains regardless of the length of time an investor has owned the fund shares.

ETFs may also be structured as investment trusts, with issued shares representing units of fractional undivided beneficial ownership of the trust. Examples are certain ETFs that track the price of gold. These trusts are treated as "grantor trusts" for tax purposes, and investors generally are treated as if they directly own a pro rata share of the underlying assets held in the trust. Investors are also treated as if they directly received their respective pro rata shares of the trust's income, if any, and directly incurred their respective shares of the expenses. Upon a sale of some or all of an investor's shares, the investor is treated as having sold the portion of his pro rata share of the trust's underlying assets at the time of the sale attributable to the shares sold. In the case of an ETF that tracks the price of gold and that is treated as a grantor trust, long-term gain from the sale of shares is taxable at a maximum rate of 28% (rather than 20%).

There are listed options on certain ETFs. Where the underlying portfolio or index is not broad-based (see page 26), the related option is taxed as a regular equity option (see page 15). The taxation of options on exchange-traded fund shares where the underlying portfolio or index is broad-based is currently uncertain and requires guidance from the IRS.

Bonds and Other Debt Instruments

The Federal income tax consequences of investing in corporate debt obligations are somewhat more complex than the tax consequences of investing in stocks. The general rule is that an investor will realize long-term or short-term capital gain, or long-term or short-term capital loss, as the case may be, on the sale of corporate debt obligations.

The general rule has been eroded, however, by a series of provisions dealing with "original issue discount," "market discount," "premium" and "short-term" obligations. In addition, special rules apply if the obligation is debt-financed (e.g., bought "on margin"). These rules typically convert capital gain to ordinary income, cause certain income to be recognized currently for tax purposes even though not yet received, or match interest income and interest expense.

Original Issue Discount

The original issue discount (OID) provisions apply to debt obligations issued at a discount from the principal amount of the obligation. The amount of OID is the excess of the stated redemption price at maturity over the issue price of the obligation. Under a de minimis exception, if a debt instrument has a very small amount of OID (less than 1/4 of 1% of the stated redemption price at maturity multiplied by the number of complete years to maturity), the OID rules do not apply. A holder of a debt obligation with OID is required to currently include in income, during the period the bond is held, the amount of OID attributable to each taxable year even though no cash is received. The OID included in income is treated as ordinary interest income. OID is computed on an "economic accrual" (constant yield) basis. The amount of OID included in income is added to the basis of the obligation.

Under the economic accrual method, OID accrues in a manner similar to the accrual of interest on deposits by financial institutions. The ratable share of OID is based on the number of days the taxpayer holds the obligation relative to the number of days until maturity.

Although OID on tax-exempt obligations is not includible in the investor's taxable income, it must still be taken into account. OID on tax-exempt obligations accrues on an economic accrual basis and increases the investor's basis in the obligation for purposes of determining gain or loss on its disposition or payment at maturity.

Zero coupon bonds are generally subject to the OID rules.

OID concepts also apply to certain redeemable preferred stock issued after October 9, 1990 with redemption premium. Like OID, redemption premium exists if the redemption price at maturity exceeds the issue price by more than a de minimis amount (same standard is applied as in the case of OID). While such stock is not debt for Federal income tax purposes, the entire amount of the redemption premium is treated as being distributed to holders on an economic accrual basis over the period that the stock is outstanding. The income tax consequences of this deemed distribution to an individual shareholder depend on the paying corporation's current and accumulated earnings. The distribution could result either in current dividend income, capital gain, or nontaxable return of capital (in the latter case with an equivalent reduction in the basis of the stock).

Market Discount

Debt obligations are subject to the market discount rules in addition to the OID rules. The market discount rules apply to debt obligations acquired at a discount in the secondary market in contrast to those issued at a discount. Except in the case of bonds issued with OID, market discount is the excess, if any, of the obligation's stated redemption price at maturity over the taxpayer's cost basis for the obligation immediately after its acquisition.

As with OID, accrued market discount is generally treated as ordinary income. Unlike OID, however, accrued market discount is not always treated as interest. For example, market discount on a tax-exempt bond is treated as taxable ordinary income, not as tax-exempt interest. Also, unlike OID, accrued market discount is not taxable until the disposition of the obligation by the taxpayer (unless the investor elects to include it in income on a current basis). The taxable amount of market discount is the amount that has accrued during the period the taxpayer has held the bond. The amount of accrued market discount treated as ordinary income is capped at the amount of gain (if any) recognized on the disposition. If the market discount is less than 1/4 of 1% of the stated redemption price at maturity multiplied by the number of complete years to maturity (after the taxpayer acquired the bond), the market discount is treated as zero.

Market discount is treated as accruing in equal daily installments; however, at the election of the taxpayer on an obligation-by-obligation basis, it can be computed on an economic accrual method.

Example:
On July 2, 2014, an investor acquires $100,000 face amount XYZ 6% bonds, due July 1, 2018, for $96,000. The obligations were issued January 1, 2012 at par. The investor sells the obligations on July 1, 2016 for $99,000. The tax consequences in the year of sale are as follows (assuming the investor has made no elections and excluding the effect of accrued coupon interest purchased and sold):

Realized gain ($99,000–$96,000)	*$3,000*
Gain treated as ordinary income	
($4,000 market discount x 729/1460)	*$1,997*
Long-term capital gain	*$1,003*

The market discount and OID provisions can apply simultaneously to an obligation. An investor will have market discount if an obligation originally issued with OID is purchased for less than the issue price plus the amount of accrued OID on the obligation since the date of issue.

Example:
XYZ Corp. $1,000 face amount 6% bonds, due September 1, 2017, were issued on September 1, 2013 for $960. On September 1, 2014, an investor acquires $100,000 face amount of the bonds for $95,913. The

amount of OID that has accrued on the bonds since the issue date is $813. Therefore, since the purchase price is less than the issue price plus the accrued OID ($96,813), the investor has market discount of $900 ($96,813–$95,913). The remaining OID on the obligation is $3,187 ($100,000–$96,813), which will be included in the investor's taxable income during the period the bonds are held (using the economic accrual method) and will increase his basis in the bonds. If the bonds are held until maturity, the investor will include the $900 of market discount in taxable income as ordinary interest income upon receiving payment of the $100,000 principal amount.

Example:
Using the prior example, assume that the bonds are instead issued by State Z. The remaining OID of $3,187 is tax-exempt interest and will increase the investor's basis in the bonds as it accrues. As in the prior example, if the bonds are held until maturity, the investor will include the $900 of market discount in taxable income as ordinary income at that time.

Investors are limited in the amount of interest expense they are able to currently deduct on indebtedness incurred to purchase or carry an obligation with market discount. A taxpayer is able to deduct the "net direct interest expense" only to the extent that it exceeds the amount of accrued market discount on the obligation for the period it is held by the taxpayer during the taxable year.

With respect to any market discount bond, net direct interest expense is the amount of interest expense incurred by the taxpayer in excess of all interest income (including OID) includible in the taxpayer's gross income for the taxable year from that bond. Any disallowed interest expense will be deductible in the year the taxpayer disposes of the bond. An investor may elect, on an obligation-by-obligation basis, to deduct the deferred interest expense in a year in which there is net interest income (in excess of interest expense) on the obligation.

An investor may avoid the limitation on interest expense deductions by electing to include market discount currently in income during each taxable year. This election, if made, applies to all market discount bonds acquired by the investor during the first taxable year to which the election applies or thereafter.

There are no similar provisions disallowing interest expense deductions on debt-financed OID obligations. However, interest expense on debt incurred to carry OID obligations is subject to the investment interest expense limitation rules (see page 38). The investment interest expense limitation also applies to interest expense on debt-financed market discount obligations, after the application of the disallowance rule described above.

Short-Term Obligations

The OID and market discount rules described above do not apply to short-term obligations. For this purpose, an obligation is short-term if the period from issue date to maturity is one year or less.

Discount on short-term obligations is not included as income by individual investors until the obligation is disposed of or paid at maturity. Any gain on disposition is treated as ordinary interest income to the extent of accrued discount (using ratable accrual unless the investor elects economic accrual) for the period the taxpayer has held the short-term obligation. Any additional gain or any loss realized is short-term capital gain or loss.

Under rules similar to those applying to market discount bonds, if a short-term obligation held by an individual investor is financed, the net direct interest expense is deferred until the discount is taken into income by the taxpayer (i.e., at disposition or maturity). A taxpayer may avoid this limitation by electing to include discount currently on all short-term obligations held.

These rules apply with respect to OID (but not market discount) on short-term non-governmental obligations and to “acquisition discount” on short-term governmental obligations (such as Treasury bills). Acquisition discount is the excess of the stated redemption price at maturity over the taxpayer’s cost basis in the obligation (effectively a combination of OID and market discount).

Amortizable Bond Premium

Bond premium is the amount paid for a bond in excess of its par value. The premium effectively reduces the yield on the bond. In the case of taxable bonds, a taxpayer may elect to amortize the bond premium over the remaining life of the bond. If made, this election is binding for all taxable bonds held or acquired in the first year to which the election applies or in subsequent years.

If the election is made, the premium is amortized on an economic accrual basis. Such amortizable premium is applied against and reduces the interest income on the bond. A taxpayer's basis in the bond is decreased to reflect the premium so applied.

In the case of tax-exempt bonds, the premium (which must be amortized) is applied to reduce the amount of tax-exempt interest on the bond and is not deductible. Basis is reduced by the amount of the amortized bond premium.

Convertibles and Exchangeables

The conversion of a convertible bond into stock of the same issuer is generally not a taxable transaction. The stock received will have the same holding period and basis as the converted bond. Any unaccrued OID will not be recognized. Accrued market discount at the time of the conversion will be recognized when the stock received is disposed of. In contrast, the exchange of debt obligations of one issuer for debt obligations or stock of another issuer (including a parent of the issuing corporation) will generally be a taxable transaction.

Exchange-Traded Notes and Similar Hybrid Instruments

A detailed discussion of the taxation of "hybrid instruments" issued in debt form is beyond the scope of this booklet. However, it has been the subject of active consideration by Congress, the

Treasury Department and the Internal Revenue Service. The use of these instruments continues to evolve, as do the tax rules that apply.

Particular attention is being paid by the government to exchange-traded notes ("ETNs"). As the name implies, these notes trade on an exchange. Although the notes are in the form of debt, investors generally are not assured of being repaid the principal amount of the note. Instead, the return on the note is tied to such things as commodity prices, foreign currency exchange rates, or a specified trading strategy tied to equities. Issuers of ETNs generally take the position that investors in these notes have no income for tax purposes until the note is sold, and that all gain and loss on disposition is long-term capital gain or loss if the note has been held for more than one year. The IRS has taken the position that certain ETNs based on foreign currencies are taxable as debt instruments and result in current income.

Conversion Transactions

The Internal Revenue Code re-characterizes as ordinary income certain amounts that would otherwise be considered capital gain (short-term or long-term) and that arise from a "conversion transaction." In a conversion transaction, the investor is in the economic position of a lender — the investor has an expectation of a return from the transaction that in substance is in the nature of interest and undertakes no significant risks other than those typical of a lender. A conversion transaction is a transaction for which substantially all of an investor's return is attributable to the time value of his or her net investment in the transaction and in which the investor (1) bought property and, at the same time, agreed to sell the same or substantially identical property for a higher price in the future; (2) created a "tax straddle" of actively traded property (see page 17); or (3) entered into a transaction that was marketed or sold as producing capital gain. The

Treasury Department is authorized to issue regulations describing other transactions it will treat as conversion transactions subject to these rules.

In general, the amount of gain re-characterized as ordinary income will not exceed the amount determined by applying 120% of the appropriate applicable Federal interest rate to the investor's net investment in the conversion transaction.

While the application of this provision to a particular transaction is often unclear (pending the issuance of official Treasury guidelines), the legislative history of this section suggests the following:

- Buying stock and writing an option where there is no substantial certainty that the holder of the option will exercise the option (e.g., long the stock, short an out-of-the-money call on the stock) is not a conversion transaction.
- An investor's net investment in a conversion transaction is the total amount invested less any amount received by the investor for entering into any position as part of the overall conversion transaction – for example, the receipt of option premium in granting an option.
- In determining an investor's net investment in a conversion transaction, the source of the investor's funds generally will not be taken into account. Thus, if an investor purchased stock for $1,000 but borrowed $900, the net investment would still be $1,000.
- Amounts that a taxpayer may be committed to pay in the future (e.g., through a futures contract) generally will not be treated as an investment until such time as the amounts are in fact committed to the transaction and are unavailable to invest in other ways. A margin "deposit" is not viewed as an investment.

Example:

On January 6, 2014, an investor enters into a long futures contract committing the investor to purchase a certain quantity of gold on March 1, 2014 for $10,000. Also on January 6, 2014 the investor enters into a short futures contract to sell the same quantity of gold on April 1, 2014 for $10,060. The investor makes the required margin deposit. On February 3, 2014 both contracts are terminated for a net profit of $20. No part of that $20 is subject to re-characterization because the investor has no investment in the transaction on which the $20 could be considered an interest equivalent return.

Investment Interest Expense and Other Investment Expenses

Subject to the application of the tax straddle rules (see page 17) and certain rules described below, an individual investor may generally deduct interest on debt incurred to purchase or carry investment property ("investment interest") in an amount up to the amount of the individual's net investment income for the year. Investment interest paid during the year that exceeds the limitation may be carried forward and may be deducted in future years (subject to the limitation applicable in that year).

Margin interest and otherwise deductible short sale expenses are treated as investment interest expense. Net investment income does not include net capital gain (net long-term capital gain minus net short-term capital loss). However, an investor can elect to include in investment income so much of his net capital gain as he chooses, but the amount of net capital gain eligible for the maximum 20% capital gain rate must be reduced by the same amount. Similarly, dividends eligible for taxation at the 20% rate are not treated as investment income unless the investor elects to treat the dividend as not eligible for the lower tax rates. See discussion on page 5. Net short-term capital gains are included in investment income.

Itemized deductions for investment advisory fees, custody and trust administration fees, subscriptions to investment advisory publications and similar expenses of producing investment income are limited. Such "miscellaneous itemized deductions," which also include certain employee business expenses, are deductible only to the extent that, in the aggregate, they exceed 2% of the taxpayer's adjusted gross income for the year. These items are not deductible at all in computing alternative minimum tax liability. The deduction for investment interest expense is not subject to these restrictions.

Individuals whose adjusted gross income exceeds a specified dollar threshold will have most of their itemized deductions reduced by an amount equal to 3% of their adjusted gross income over that threshold. For 2015, threshold is $258,250 for single filers ($309,900 for married taxpayers filing jointly). These thresholds are adjusted annually for inflation. Investment interest expense (such as margin account interest) is excluded from the list of itemized deductions that are subjected to this limitation. In no event are allowable itemized deductions that are subject to this limitation reduced by more than 80%. The limitation, which applies for regular tax purposes but not for purposes of the AMT, is applied after the application of the 2% floor on miscellaneous itemized deductions discussed above.

Appendix I

In-the-Money Qualified Covered Calls For Stock Priced $25 or Less ($2.50 intervals)

Applicable Stock Price ($)	Strike Price ($)
5.01 to 5.88	5
5.89 to 7.50	None
7.51 to 8.82	7.50
8.83 to 10.00	None
10.01 to 11.76	10
11.77 to 12.50	None
12.51 to 14.70	12.50
14.71 to 15.00	None
15.01 to 17.50	15
17.51 to 20.00	17.50
20.01 to 22.50	20
22.51 to 25.00	22.50

In-the-Money Qualified Covered Calls For Stock Priced $25 or Less ($1.00 intervals)

Applicable Stock Price ($)	Strike Price ($)
2.51 to 2.94	2.50
2.95 to 4.00	None
4.01 to 4.70	4.00
4.71 to 5.00	None
5.01 to 5.88	5.00
5.89 to 6.00	None
6.01 to 7.00	6.00
7.01 to 8.00	7.00
8.01 to 9.00	8.00
9.01 to 10.00	9.00
10.01 to 11.00	10.00
11.01 to 12.00	11.00
12.01 to 13.00	12.00
13.01 to 14.00	13.00
14.01 to 15.00	14.00
15.01 to 16.00	15.00
16.01 to 17.00	16.00
17.01 to 18.00	17.00
18.01 to 19.00	18.00
19.01 to 20.00	19.00
20.01 to 22.50	20.00
22.51 to 25.00	22.50

Some low priced stocks have listed options in $1 intervals and others have $2.50 intervals (or a hybrid of $1 and $2.50 intervals). Some stocks may have listed options with $0.50 intervals. Investors need to determine which strike price intervals are available for options on a particular stock.

Appendix II

The chart beginning on the next page summarizes the treatment of certain transactions for Federal income tax purposes. The description below is not binding upon the Internal Revenue Service and, accordingly, no assurance can be given that the Service will not challenge such treatment or, if challenged, that such treatment would be upheld.

Legislation may be enacted by Congress or regulations may be issued by the Internal Revenue Service in the future that may result in tax treatment different from that set forth below. In particular, IRS guidance with respect to the application of the constructive sale rule to option transactions, when issued, may significantly impact the tax treatment described in this Appendix II.

Investors are strongly advised to consult their tax advisors in considering the tax consequences of transactions in light of their own specific circumstances.

Effects of Various Strategies

	Positions	Effect on Holding Period	Deferral of Loss (1)	Capitalization of Interest and Carrying Charges
1.	**Long Stock-Short Stock** (substantially identical or substantially similar) (2)	Terminate if stock held short-term	Yes	Yes
2.	**Long Stock-Short Stock** (not substantially identical, not substantially similar)	No Effect	No	No
3.	**Long Stock-Short Call** (not qualified covered call)			
a.	**stock held**: short-term	Terminate	Yes	Yes
b.	**stock held:** long-term	**(3)**	Yes	Yes
4.	**Long Stock-Short At-the-Money or Out-of-the-Money Qualified Covered Call**			
a.	**long stock:** gain or loss position **time of writing call:** not relevant **call closed:** same year as stock sold, gain or loss on call not relevant	No Effect	No	No

	Positions	Effect on Holding Period	Deferral of Loss (1)	Capitalization of Interest and Carrying Charges
b.	**long stock:** gain position **time of writing call:** not relevant **call closed:** at loss, year preceding disposition of stock **days stock held after call closed:** less than 30 days **(4)**	No Effect	Yes	No
c.	**long stock:** gain position **time of writing call:** not relevant **call closed:** at loss, year preceding disposition of stock **days stock held after call closed:** 30 days or more **(4)**	No Effect	No	No
d.	**long stock:** loss position **time of writing call:** not relevant **call closed:** at gain, year preceding disposition of stock **days stock held after call closed:** not relevant	No Effect	Not Applicable	No
e.	**long stock:** loss position **time of writing call:** not relevant **call closed:** at gain, year subsequent to disposition of stock **days option held after stock sold:** less than 30 days **(4)**	No Effect	Yes	No
f.	**long stock:.** loss position **time of writing call:** not relevant **call closed:** at gain, year subsequent to disposition of stock **days option held after stock sold:** 30 days or more **(4)**	No Effect	No	No

	Positions	Effect on Holding Period	Deferral of Loss (1)	Capitalization of Interest and Carrying Charges
5.	**Long Stock-Short In-the-Money Qualified Covered Call**			
a.	**long stock:** gain or loss position **time of writing call:** stock held long-term **call closed:** same year as stock disposed, gain or loss on call not relevant	**(3)**	No	No
b.	**long stock:** gain or loss position **time of writing call:** stock held short-term **call closed:** same year as stock sold, gain or loss not relevant	Suspend	No	No
c.	**long stock:** gain position **time of writing call:** stock held long-term call closed: at loss, year preceding disposition of stock **days stock held after call closed:** less than 30 days **(4)**	**(3)**	Yes	No
d.	**long stock:** gain position **time of writing call:** stock held long-term **call closed:** at loss, year preceding disposition of stock **days stock held after call closed:** 30 days or more **(4)**	**(3)**	No	No
e.	**long stock:** gain position **time of writing call:** stock held short-term **call closed:** at loss, year preceding disposition of stock **days stock held after call closed:** less than 30 days **(4)**	Suspend	Yes	No

continued on following page

	Positions	Effect on Holding Period	Deferral of Loss (1)	Capitalization of Interest and Carrying Charges
f.	**long stock:** gain position **time of writing call:** stock held short-term **call closed:** at loss, year preceding disposition of stock **days stock held after call closed:** 30 days or more **(4)**	Suspend	No	No
g.	**long stock:** loss position **time of writing call:** stock held long-term **call closed:** at gain, year preceding disposition of stock **days stock held after call closed:** not relevant	No Effect	Not Applicable	No
h.	**long stock:** loss position **time of writing call:** stock held short-term **call closed:** at gain, year preceding disposition of stock **days stock held after call closed:** not relevant	Suspend	Not Applicable	No
i.	**long stock:** loss position **time of writing call:** stock held long-term **call closed:** at gain, year subsequent to disposition of stock **days option held after stock sold:** less than 30 days **(4)**	No Effect	Yes	No
j.	**long stock:** loss position **time of writing call:** stock held long-term **call closed:** at gain, year subsequent to disposition of stock **days option held after stock sold:** 30 days or more (4)	No Effect	No	No

	Positions	Effect on Holding Period	Deferral of Loss (1)	Capitalization of Interest and Carrying Charges
k.	**long stock:** loss position **time of writing call:** stock held short-term **call closed:** at gain, year subsequent to disposition of stock **days option held after stock sold:** less than 30 days **(4)**	Suspend	Yes	No
l.	**long stock:** loss position **time of writing call:** stock held short-term **call closed:** at gain, year subsequent to disposition of stock **days option held after stock sold:** 30 days or more **(4)**	Suspend	No	No
6.	**Long Stock-Long Call**	No Effect	No	No
7.	**Long Stock-Short Put**	No Effect	No	No
8.	**Long Stock-Long Put**	Terminate (5)	Yes	Yes
9.	**Short Stock-Short Put**	Not Applicable	Yes	Yes
10.	**Long Call-Short Call**	Terminate (5)	Yes	Yes
11.	**Long Call-Long Put**	Terminate (5)	Yes	Yes
12.	**Long Call-Short Stock**	Terminate (5)	Yes	Yes
13.	**Long Call-Short Put**	No Effect	No	No
14.	**Long Put-Short Put**	Terminate (5)	Yes	Yes
15.	**Long Put-Short Call**	No Effect	No	No
16.	**Short Call-Short Put**	Not Applicable	Yes	Yes
17.	**Long Put-Short Stock**	No Effect	No	No
18.	**Short Call-Short Stock**	Not Applicable	No	No

continued on following page

	Positions	Effect on Holding Period	Deferral of Loss (1)	Capitalization of Interest and Carrying Charges
19.	**Long Portfolio of Stock-Short Broad U.S. Stock Index Future** ("substantial overlap")(6)	Terminate (5)	Yes	Yes
20.	**Long Portfolio of Stock-Short Call on Broad U.S. Stock Index** ("substantial overlap")(6)	Terminate (5)	Yes	Yes
21.	**Long Portfolio of Stock-Short Call on Broad U.S. Stock Index Future** ("substantial overlap")(6)	Terminate (5)	Yes	Yes
22.	**Long Portfolio of Stock-Short Broad U.S. Stock Index Future** (not "substantial overlap")(6)	No Effect	No	No
23.	**Long Portfolio of Stock-Short Call on Broad U.S. Stock Index** (not "substantial overlap")(6)	No Effect	No	No
24.	**Long Portfolio of Stock-Short Call on Broad U.S. Stock Index Future** (not "substantial overlap")(6)	No Effect	No	No

Notes

1. When there are offsetting positions in a straddle, losses realized on the closing of a position are deferred to the extent of the unrecognized gain at the end of the year in "offsetting positions" to the loss position. The deferred loss may be deductible by the investor in a subsequent year.

2. If the stock is appreciated, and subject to certain exceptions, gain is recognized as if the stock were sold at its fair market value on the date the short sale is entered into and immediately repurchased. The basis of the appreciated position is increased by any gain realized, and a new holding period begins as if the position had been acquired on the date of the constructive sale. As a result of

the enactment of the 2004 Act, long stock versus short stock may now be treated as an offsetting position for purposes of the tax straddle rules (see note 1 and pages 17-19). If the stock has been held long-term when the short sale is entered into and the short sale is closed at a loss, the loss is automatically a long-term loss.

3. If the stock is held long-term at the time the call is written, any loss on the call will be treated as a long-term capital loss.

4. Only days on which the stock is held with no offsetting position will generally be counted. However, the holding period continues to run while the investor is the writer of at-the-money or out-of-the-money qualified covered calls (but not in-the-money qualified covered calls).

5. Holding period is terminated if the long stock or long option (or long portfolio of stock, as the case may be) is held short-term at the time the investor enters into the offsetting position; the holding period of any position that is part of a straddle does not begin earlier than the date the investor no longer holds an offsetting position. However, if the position has been held long-term when the straddle is created, it will continue to be held long-term, but any loss on any offsetting positions will also be long-term.

6. When the stocks contained in a broad-based stock index and a portfolio of stocks held by the investor "substantially overlap," offsetting positions in the portfolio of stocks and in instruments based on that index will be subject to the tax straddle rules (including the loss deferral rule) and the "mixed" straddle rules. Treasury regulations provide an objective mechanical test to determine the amount of over-lap between the portfolio and the index and the extent to which the tax straddle rules apply.

For More Non-Tax-Related Information

BATS Exchange
www.batstrading.com

BOX Options Exchange
www.bostonoptions.com

Chicago Board Options Exchange (CBOE)
www.cboe.com

International Securities Exchange (ISE)
www.ise.com

MIAX Options Exchange
www.miaxoptions.com

NASDAQ
www.nasdaqtrader.com

NYSE
www.nyse.com

The Options Clearing Corporation (OCC)
www.theocc.com

The Options Industry Council (OIC)
www.OptionsEducation.org

For More Tax-Related Information

Keyes, “Federal Taxation of Financial Instruments and Transactions” (Warren Gorham and Lamont)

Conlon and Acquilino, “Principles of Financial Derivatives” (Warren, Gorham and Lamont)

Kramer, “Financial Products, Taxation, Regulation and Design” (Panel Pub.)

Shapiro, “Taxation of Equity Derivatives” (BNA Tax Portfolio #188)