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Simple Rules for Using Options to Trade the "ETF TREND TRADING SYSTEM"! June 21, 2010

System Rules:

- ETF entry and exit points are determined by the "ETF Trend Trading System", but ONLY for use on 5BP Break out Trades!

- When the system signals to buy or short an ETF, instead buy a call or put option. How many to buy depends on your risk tolerance. Remember, each call option is equivalent to 100 shares of the ETF!

  CONSERVATIVE: Choose how many calls to buy, based on how many SHARES of the ETF the system indicates, and round up. (If the system tells you to buy 121 shares of the SPY, instead, buy 2 calls options.)

  AGGRESSIVE: Spend as much DOLLARWISE on call options as the system indicates to spend on the purchase of the ETF, rounding down the number of calls. (If the system tells you to buy $1,500 worth of the IWM, instead buy $1,500 worth of call options on the IWM, if the call option costs $1,100, buy 1.)

  It's highly recommended to start at the conservative level, as at the aggressive level you're getting into more "speculation" than "stock replacement" levels!

- ONLY buy calls that are “In the Money” and are at least 3+ months out from expiration. For example, if today is January 5th, I’d skip past on the January, February, and March options, and look to buy April. If that month isn’t available, take the next month out.

- Select an option that is at least 3 series “In the Money” AND has a Delta value of .75 to .85. For example, if the ETF is the SPY, and it’s trading at 110, and the options available are 110, 109, 108, 107, 106, etc. 3 series “In the Money” would be 107.

- When the ETF Trend Trading System hits a profit target or stop loss on the underlying ETF, we immediately close the option position. You can also setup what are called “conditional” orders inside of ThinkorSwim and TradeStation.

- At no time do we hold our options into the final month before expiration. Ideally, liquidate the position the Wednesday before the one-month expiration date. Roll the total amount of money from the liquidated option to a new position, following the rules above.