GOVERNANCE MATTERS

building shareholder value

CEO pay – It's even higher than you think

Valuation of executive options in Australia

Research Paper prepared by ISS Australia

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1. Executive Summary

Background

To ascertain how real or otherwise the reported values of long-term incentives granted to CEOs are, institutional governance advisor ISS Australia reviewed the results of the value gained or lost by CEOs of top 100 Australian companies over the past 16 months as a result of options either being exercised or lapsing due to performance hurdles not being met. (By 'options' we mean traditional market exercise price options, and all other long-term equity incentives such as 'performance rights' — which are in fact options with an exercise price of zero.)

The study compared the value the company attributed to options at the time they were granted to the CEO ('fair value') to the actual value realised by the CEO when the options were exercised years later ('realised value'). This study continues and broadens earlier work by ISS — released last year — that compared the value of long-term incentives realised by CEOs on exercise with the reported fair value at the time the incentives were granted.

Key findings

- The 2006 study shows the average 'fair value' attributed to options at grant date is only 26% of the actual value realised by the CEO. The 2005 study found the average 'fair value' attributed to options at grant date was 31% of the actual value realised by the CEO.
- Of the 70 options tranches reviewed, 46 (66%) were exercised and 24 (34%) lapsed.
- The value realised by the CEO upon exercise of the options was greater than the fair value attributed to the options exercised in 45 of the 46 option exercises reviewed by ISS Australia. This is in line with ISS' earlier research covering the four years to 2005, which also found that the reported fair value was less than the value realised on exercise on all but one occasion.

	2005 study	2006 study
Period covered	Options exercised between April 2002 – April 2005	Options exercised between May 2005 – August 2006
'Fair value' as proportion of 'realised value' (average)	31%	26%
Number of cases where realised value > fair value (where options exercised)	23 out of 24 cases	45 out of 46 cases

- On 13 occasions the actual value realised by the CEO on the exercise of options was more than five times greater than the fair value of the same options as disclosed by the company. On one occasion, the realised value was 33.4 times greater than the fair value.
- 11 CEOs held 24 tranches of options that lapsed during the study period. The average fair value of options held by a CEO that lapsed due to performance hurdles not being met (or due to termination of contract) was $1,204,052. As above, this was the average value calculated and disclosed by the company at the date the options were granted.
- Past and present disclose rules around option valuation are inadequate, as they do not require companies to disclose the size of any discount applied to the fair value of options granted to an executive to allow for the possibility of the options not vesting.
- Of the 46 vested option tranches exercised, 30 were exercised following the achievement of a relative TSR hurdle. Of the 24 that lapsed, 22 were subject at least in part to a relative TSR hurdle; of these, three had in fact vested but were cancelled by the company following the resignation of the CEO.

2. Options Valuation Mismatches in Australia

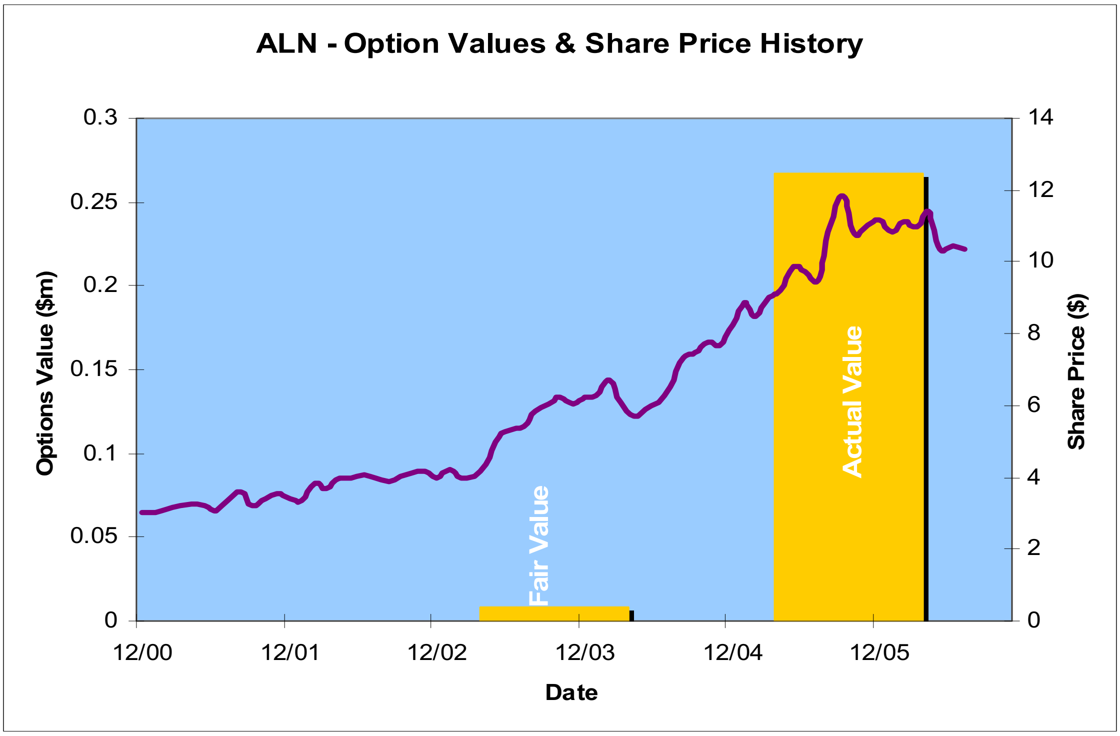
The first part of the study examined the 24 S&P/ASX 100 companies that had disclosed the 'fair value' of options since 1999, and whose CEO had exercised options between May 2005 and 16 August 2006. A total of 46 separate exercises of options were included in the sample. The sample period was chosen as ISS had in prior research reviewed the realised value of options exercised by Top 100 company CEOs during the period April 2002 to April 2005.

ISS Australia's study revealed that the average 'fair value' (or 'grant date' value) of options exercised by a CEO was $931,713. This was the average value calculated and disclosed by the company at the date the options were granted. But when the executive actually exercised the options several years later, the average gain realised by the executive was $3,572,513.

With only one exception, the value of the incentives that vested was higher than the fair value disclosed by the company at the time of grant.

Case study: Alinta

The largest difference in value occurred at Alinta. The company granted Bob Browning 300,000 options in 2003. Mr Browning exercised 40,000 of the options in 2005, and so this analysis focuses on that tranche of 40,000 options.



Alinta's 2003 annual report on page 38 disclosed a 'fair value' per option of $0.20. This put a total value on the tranche of $8,000. The options were issued with a performance hurdle requiring Alinta's total shareholder return (TSR) to be at least equal to the median TSR of the S&P/ASX 200 and at least equal to the average TSR of peer utilities companies. Alinta also disclosed that one of the factors used in valuing the options was the 'tenure risk inherent in the options'.

When Mr Browning exercised the options in 2005, Alinta's share price was $11.20. The exercise price he paid to transform the options into shares was $4.5177 per option.[1] Mr Browning's actual gain on exercising the options (assuming the shares he sold on exercise of the options were sold at the closing price on the day of exercise) was therefore $6.6823 per option, or $267,292 for the whole tranche.

The total value actually derived by Mr Browning (before tax) from the 40,000 options exercised was 33.4 times greater than the value originally placed on the options by Alinta. Under Australia's disclosure rules (see Section 4 of this report), it was the 'fair value' as calculated at grant-date, rather than the actual value derived by the CEO, that the company included as part of Mr Browning's remuneration disclosed to shareholders. In fact, the value Mr Browning received on exercising 40,000 options was greater than the fair value of all 300,000 options he was granted in 2003. The remaining 260,000 options have all vested and, based on Alinta's closing share price of $10.90 on 23 August 2006, are now worth $1.659 million — compared with the value of $52,000 Alinta disclosed when they were granted to Mr Browning in 2003.

It should be noted that Alinta's share price did increase by nearly 130% over the 30 months between the options being granted to Mr Browning and the time they were exercised. The value received by Mr Browning is therefore in line with returns to shareholders. The point is not that the value received by Mr Browning on exercise was excessive, but rather too often there is a complete mismatch between the values calculated by companies at grant date and the value actually derived by senior executives on vesting. In the case of Alinta, when assessing the appropriateness of Mr Browning's remuneration package in 2003, investors were told that the total value of the 300,000 options granted was $60,000 — not the $1.9 million that the entire tranche is now worth.

Other cases of substantial mismatch

Alinta is not the only S&P/ASX 100 company where the reported fair value of CEO options has been substantially less than the value actually realised on exercise. A full list of the companies included in the ISS sample, along with the fair value of the options at time of grant and the value of the options realised, is attached as Appendix 1. The five biggest mismatches between grant-date value and actual value on exercise were (in order): Alinta; AXA with one tranche of options granted to outgoing CEO Les Owen in 2003 being realised for 9.6 times fair value; Bluescope, with a 2002 tranche of options to Kirby Adams being realised for 9.1 times fair value; QBE, with a 2003 grant of options to Frank O'Halloran being realised for 8.7 times fair value; and Santos, with a 2000 grant of options to John Ellice-Flint being exercised for 7.6 times fair value.

Shareholders in all five companies, as shown by the graphs in Appendix 3, have enjoyed substantial gains in share price over the period between the options being granted and exercised; although the gains enjoyed by shareholders have, in percentage terms, been a small fraction of the gain on fair value enjoyed by the CEOs.

Table 1: Top five cases of options valuation mismatch

CEO	Co.	Total Fair Value	Total Realised Value	RV/FV
Bob Browning	ALN	$8,000	$267,292	33.41
Les Owen	AXA	$166,650	$1,598,931	9.59
Kirby Adams	BSL	$480,690	$4,380,165	9.11
Frank O'Halloran	QBE	$192,040	$1,673,461	8.71
John Ellice-Flint	STO	$750,000	$5,690,000	7.59

[1] The original exercise price was $4.9182 but this was reduced due to a rights issue in March 2004.

The persistent mismatch between grant-date value and actual value on exercise begs the question as to why this occurs (particularly as the comparatively low values calculated and reported as at date of grant occurred prior to the requirement for companies to expense grants of options to executives and other staff).

Potential explanations for low grant-date valuation

There are several potential explanations for the mismatch between grant-date value and actual value on exercise:

- Companies and their advisers may be systematically underestimating the probability of vesting and hence 'over-discounting' options values. Over-discounting the value of options decreases the reported size of CEO remuneration packages.
- The strong rise in stock prices over the past three years may not have been anticipated by grant-date valuation models.
- The adoption of more demanding performance hurdles on option grants — specifically, hurdles requiring companies to outperform 75% of their peers in order for all options to vest — may have meant that when options vest under these schemes, their actual value is far higher than the fair value at grant date.
- Going forward, given that IFRS requires companies to expense the value of options in the Profit & Loss Statement, the lower the value ascribed to options at grant date, the lower the hit to the bottom line.

TSR hurdles and option value

ISS reviewed the 13 cases where the realised value of grants was more than five times the fair value disclosed at grant date. This was done to test whether these cases of substantial mismatch in value were due to the impact of TSR performance hurdles requiring companies to substantially outperform their peers for incentives to vest. Such hurdles may explain some of the difference between grant-date value and actual value on exercise, given that incentives will only vest against such hurdles in the event of substantial outperformance (and presumably, strong share price gains and/or dividend payments).

The findings of this review suggest that the valuation mismatch was not due to the difficulty of attempting to value options subject to relative TSR hurdles. Specifically, of the 13 different option exercises where the reported fair value was less than one-fifth the realised value:

- In four cases the options exercised were subject to demanding TSR hurdles requiring a company to outperform 75% or more of its peers in order for all of the options to vest.
- In two cases, the options had no performance hurdles outside of the exercise price and continued service.
- In four more cases all the options vested when the company's TSR beat that of the median peer or that of an index. This is known as a 'cliff vest' hurdle.
- In two cases the hurdle allowed options to vest even where the company's TSR was below that of the median company in the peer group.
- In one case options vested after the company beat an absolute TSR hurdle.

Discounting for the probability of hurdles being satisfied

Regardless of the reasons for it, the discrepancy between the reported fair values and the realised values distorts the true remuneration received by many CEOs. At the very least, the true value of options given to CEOs remains difficult for investors to judge — especially given many companies, like Alinta, applied an undisclosed discount when valuing options to account for the probability of a performance hurdle not being attained.

The headline option value derived using Black Scholes or binomial pricing is typically discounted by a certain percentage to allow for the possibility of performance hurdles not being achieved. Some companies also discount for the possibility of the executive resigning (and the options lapsing as a result), and for the fact that executive options are not tradeable in the market.

In some cases, the gap between fair and realised values suggests that the discount for performance hurdles being used is extremely, and potentially unrealistically, large. For example, Telstra in its 2006 Financial Report discloses that the fair value of options granted to senior executives that are subject to an (undisclosed) TSR hurdle has been discounted by 85%. That is, Telstra has assumed there is only a 15% chance of the TSR hurdle being met.[2] Telstra is unusual in that it *does* disclose the size of the discount it is applying when valuing the options granted to executives.

Persistent sizeable mismatches between grant-date value and actual value of options granted to senior executives suggests that, at a minimum, disclosure rules should be tightened:

- Companies should be required to disclose not only that a discount has been applied, but the size of the discount itself.
- In many cases shareholders would consider the fact that a company thinks there is a greater than 50% chance of performance hurdles not being met as meaningful information.
- The discount is already implicitly disclosed to the market through the disclosure of the fair value of the options. Requiring companies to disclose the size of any discount applied for the probability of hurdles not being met would simply provide shareholders with more information when assessing the true value of executive incentives.

Requiring the disclosure of any discount factor applied to the fair value of the options would also allow investors to form their own view as to what portion of executive pay was at risk. In 2005 an average of 40.7% of executive pay across S&P/ASX 100 companies was reported to be 'at risk'. The valuation issue is therefore an important one for investors as gains made on the exercise of an option are not regarded as executive remuneration for the purposes of disclosing executive pay.

[2] No options granted in 2005/06 by Telstra are included in this survey as none of them have vested. The example is used for illustrative purposes only.

3. The Downside of Australian Executive Options

In the sample period, 11 chief executives had 24 different tranches of option instruments lapse.[3] In two cases options expired when the share price was higher than the option exercise price.

The average value of options held by a CEO that lapsed due to performance hurdles not being met (or due to resignation or termination of contract) was $1,204,052. As above, this was the average value calculated and disclosed by the company at the date the options were granted.

However, this figure is distorted by the case of former Amcor CEO, Russell Jones, half of whose lapsed options were in fact vested options that the board decided to cancel when Mr Jones left the company (see below). If Mr Jones is excluded from the sample, and only options which lapsed following non-satisfaction of performance hurdles are included, the average value of options lapsed per CEO was $683,600.

Case study: Amcor

The largest amount foregone by a CEO was $6,408,579. This was the former CEO of Amcor, Russell Jones, who had 6 million options cancelled following his resignation from Amcor in the aftermath of allegations of anti-competitive behaviour. This included 3 million options that had in fact already vested but had not yet been exercised which were cancelled by the board. These options, had they been exercised immediately prior to Mr Jones' departure from Amcor, would have been worth $5.61 million. The aggregate fair value of these vested options was $1.373 million.

Outside of Mr Jones, the largest value foregone was by Westpac CEO, David Morgan. Dr Morgan had 972,114 options with a total reported value of $2,270,141 lapse. However, as noted below and in Appendix 1, Dr Morgan also had several tranches of options vest during the period.

The findings indicate some CEOs can justifiably complain their reported remuneration actually exaggerates their take-home pay. Dr Switkowski during the sample period saw options with a fair value of more than $1.7 million lapse, all of which were included in his disclosed remuneration in 2003/04.

However, the smaller numbers of CEOs whose options have lapsed — 11 as opposed to 24 CEOs whose options vested and were exercised — and the discrepancy between the aggregate fair value of options lapsed and the value realised from vested options, indicate that S&P/ASX 100 companies have in the past tended to under-state CEO remuneration, not over-state it with the inclusion of 'illusory' long-term incentives. This is confirmed by examining cases where CEOs had options lapse and options vest during the survey period.

CEOs who had some options vest and some lapse

ISS identified four cases where a CEO had exercised vested options during the sample period and also had some options lapse. These were the CEO of Westpac, Dr Morgan; the CEO of Qantas, Geoff Dixon; the CEO of BHP, Chip Goodyear; and the former CEO of Mayne (prior to its de-merger), Stuart James. In three of these four cases the total realised value of all options exercised was greater than the total fair value of the exercised options plus the fair value of the options that lapsed.

In aggregate, Dr Morgan realised $8,028,004 from exercising vested options during the sample period and had options with a fair value of $2,270,141 lapse. The options Dr Morgan exercised had an aggregate fair value of $2,855,859. Despite having options lapse, Dr Morgan still realised almost $3 million more than the total fair value of all options exercised or lapsed during the sample period.

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[3] Information about lapsed options was taken from annual reports for financial years ending on or after 30 June 2005.

In aggregate, Mr Dixon realised $814,780 from exercising options during the sample period and had options with a fair value of $218,046 lapse. The total fair value of all instruments granted to Mr Dixon that were exercised or that lapsed during the sample period was $1,187,320 — making Mr Dixon the only CEO in the sample for whom the reported fair value of options was higher than the value realised on the exercise of options.[4]

In aggregate, BHP Billiton's Mr Goodyear realised $1,769,872 from exercising options during the sample period and had options with a fair value of $99,013 lapse. The total fair value of all Mr Goodyear's options that were exercised or that lapsed during the sample period was $486,005. So, despite having options lapse, Mr Goodyear still realised almost $1.3 million more than the total fair value of all options exercised or lapsed during the sample period.

In aggregate, Mayne's former CEO Mr James realised $1,600,400 from exercising options during the sample period and had options with a fair value of $190,400 lapse. The total fair value of all Mr James' options that were exercised or that lapsed during the sample period was $1,136,800. So, despite having options lapse, Mr James still realised $450,000 more than the total fair value of all options exercised or lapsed during the sample period.

All of Mr James' options that vested were due to the board of Mayne exercising discretion to enable vesting due to the demerger. In explaining its decision to allow early vesting of all Mr James' outstanding options, the Mayne board stated that the 'vesting conditions … have been satisfied to date'. Half of the 280,000 options that were allowed to vest early by the Mayne board had only been tested against the three-year earnings per share performance hurdle for one year at the time of vesting.

[4] Most of the value realised by Mr Dixon and all of the value foregone related to long term entitlements granted in 2000 which did not convert into Qantas shares on a one-for-one basis. After these entitlements were granted, Qantas in the 2001 annual report stated they had a fair value of $0.89 per entitlement; in the 2003 report the fair value per entitlement was reported as being $0.82. ISS has used the original fair value of $0.89.

4. Current Disclosure Requirements

There are three sets of rules that now require listed companies to disclose the value of executive share options in annual reports. The first is accounting standard AASB 2, which governs how share-based payments are valued for the purposes of expensing them in the statement of financial performance (Profit & Loss Statement); the second is AASB 124, which governs the reporting of executive remuneration; and the third is section 300A of the Corporations Act. The way in which options are valued has changed slightly under AASB 2 relative to the old regime under AASB 1046 (companies have been required to value options under AASB 2 for financial years ending on or after 31 December 2005).

AASB 124 is the relevant standard for the purposes of disclosing CEO pay in the Remuneration Report, but it does not contain details about valuation of options. Instead, it effectively cross-refers to AASB 2 for this purpose.

AASB 2 states that how and when an option will be valued depends on the nature of the performance conditions attached to the option. Options which have a 'market condition' on performance — where the performance hurdle is linked to share price performance (for example, TSR against a peer group) — must be valued at grant date, although companies are able to take into account a discount for the probability of the options not vesting. However, companies must then continue to include in an executive's remuneration the fair value of all options granted (amortised across the vesting period), regardless of whether or not the options are likely to vest. Options which have other types of vesting conditions (for example, earnings per share or continued service) are valued at grant date but the number of options of a particular tranche that are included in any particular year's remuneration are then altered to reflect the present probability of those options vesting in future years. Under former AASB 1046, companies were expected to value all options, regardless of the performance hurdles, at grant date, and were not allowed to discount the fair value for the probability of an option not vesting. Instead, companies were expected to account for the probability of options vesting by adjusting the total number of options included in remuneration. **However, it should be noted that all the options exercised in 2005/06 were granted (and therefore valued) prior to the introduction of AASB 1046 or AASB 2.**

Another difference between AASB 2 and former AASB 1046 is the treatment of options for the purposes of the statement of financial performance: AASB 1046 did not require options to be treated as an expense whereas AASB 2 requires the fair value of options granted to be expensed. Perhaps as a result, whereas AASB 1046 explicitly stated:

"Gains made when a vested option or right is exercised are not remuneration under this Standard and are not required to be disclosed" (para 6.3.9);

AASB 2 instead requires companies to report each year for all employees:

"For share options exercised during the period, the weighted average share price at the date of exercise." (para 45 c) (Under the standard, companies are able to report a weighted average for all options exercised during the year.)

AASB 124, which governs the reporting of executive remuneration, requires companies, at the end of each financial year, to disclose the number of options exercised during the year as well as the number of options that lapsed, but not the value realised on exercise.

However, section 300A(1) of the Corporations Act requires companies not only to disclose the number of options exercised during the year, but also the fair value of any options granted during the year and the value of options lapsed during the year. The Act requires options to be valued at date of grant in accordance with 'any applicable accounting standards'.

Methods commonly used to calculate value at the grant date include the Black-Scholes and Binomial models. Some companies, particularly those with options with TSR performance hurdles, also use Monte-Carlo simulations to estimate the fair value of options at time of grant.

AASB 2 says whatever option-pricing model is used there are six variables that must be taken into account: Exercise-price, option life, current price of the underlying shares, expected volatility, expected dividends and the risk-free interest rate for the expected life of the instrument.[5]

[5] However, AASB 2 allows companies more flexibility in valuing shares, as opposed to options, that are granted as part of remuneration. It is not known whether zero-priced options would be treated as shares or options under AASB 2 (the definition of a share option in the standard refers to options as being a contract giving the 'holder the right … to subscribe for the entity's shares at a fixed or determinable price for a specified period of time'). This report has used options to denote traditional options as well as zero-priced options and any other form of equity-based remuneration.

5. Methodology

- The study reviewed all current constituents of the S&P/ASX 100.
- The criteria for inclusion in the analysis were:
    1. The CEO must have exercised options some time in the last 16 months. ISS used only the CEO per company (although for some companies there was more than one executive director for whom a calculation could have been conducted).
    2. In respect of the options exercised, the company must have disclosed a 'fair value' as at the date of grant. Not all companies disclosed the value of options at grant date before 2003. It was not until 2003 that ASIC insisted that the (pre-remuneration report) section 300A of the Corporations Act mandated disclosure of grant-date value. This criterion eliminated many companies from the study.
    3. Where a CEO had exercised options and a fair value for those options was disclosed in an annual report after 30 June 2003, ISS estimated the fair value of earlier options granted from the disclosures made in the later annual reports. This included 'reverse-engineering' the fair value from the amortised value of options granted disclosed in the remuneration table for the CEO and other executives, although this was only done if sufficient data existed to establish the fair value of different tranches of options.
    4. The company must have disclosed sufficient information to enable a calculation of 'actual value' at the time of vesting.
    5. For options that lapsed, ISS reviewed annual reports of top 100 companies for financial years ending on or after 30 June 2005 to determine whether any options granted to the CEO had lapsed. ISS also reviewed directors' interests filings with the ASX to determine if options had lapsed, although some S&P/ASX 100 companies did not inform the market when options lapse (despite ASX Listing Rule 3.19A, which requires directors' interests in the securities of a company to be disclosed within five business days of the change occurring). The particular tranche that lapsed was determined through information contained in annual reports and directors' interest notices. As with option exercises, ISS excluded any options granted where the fair value at grant date could not be determined.

  24 companies from the S&P/ASX 100 met these criteria for options that were exercised while 11 companies met the criteria for options that lapsed. A total of 31 different companies are included in the sample (i.e. CEOs at four companies both exercised options and had options lapse, although only two CEOs exercised options and had options lapse from the same grant of options).

- Companies and their executives who were included in the study are listed in the accompanying appendices.
- 'Actual value' was calculated as: [Number of options exercised x Share price at time of exercise] minus [Number of options exercised x Exercise Price]
- For the price of the company's shares at the time the options were exercised, we used either:
    - The exact price at which the executive sold the resulting shares where this was disclosed; or
    - Where that was not disclosed, or where the executive did not sell the resulting shares, we used the closing share price on the day the options were exercised.
- In some cases the exercise price at the time the executive exercised the options was different to the exercise price disclosed in the first annual report following the grant of the options. This could be due to a stock split (e.g. Patrick Corporation) or share buy backs or other capital restructurings. We used the exercise price actually paid by the executive at the time of vesting.

- Multiple options tranches were aggregated to provide the average fair value, the average realised value and the average fair value foregone for each CEO. Each individual tranche of options exercised or lapsed is disclosed in the appendices.

Appendix 1 - Vested & exercised incentives

CEO	Co.	Granted	Exercised	Hurdle Type	No. exercised	Total Fair Value (FV)	Realised Value (RV)	RV/FV
Robert Browning	ALN	08-May-03	12-Sep-05	TSR: Outperform index	40,000	$8,000	$267,292	33.41
John McFarlane	ANZ	31-Dec-01	08-Aug-05	TSR: Outperform index	500,000	$1,340,000	$2,538,400	1.89
John McFarlane	ANZ	31-Dec-01	03-Jul-06	TSR: Outperform index	500,000	$1,340,000	$4,945,000	3.69
John McFarlane	ANZ	31-Dec-02	04-Jul-06	TSR: Outperform index	500,000	$1,045,000	$4,975,000	4.76
Brendan Hopkins	APN	24-May-03	26-May-06	EPS	1,000,000	$720,000	$1,820,000	2.53
Les Owen	AXA	14-May-02	11-Aug-06	TSR: Outperform index	221,840	$168,598	$730,785	4.33
Les Owen	AXA	14-May-02	14-Aug-06	TSR: Outperform index	399,410	$303,552	$1,349,047	4.44
Les Owen	AXA	24-Apr-03	16-Aug-06	TSR: Outperform index	378750	$166,650	$1,598,931	9.59
Derek O'Neil	BBG	18-Jun-01	16-Sep-05	TSR: Outperform median	13,606	$20,817	$111,841	5.37
Derek O'Neil	BBG	23-Aug-02	16-Sep-05	TSR: Outperform median	8,333	$24,415	$41,831	1.71
Chip Goodyear	BHP	08-Nov-01	5-May-05	TSR: Relative, sliding scale	53,600	$193,496	$884,400	4.57
Chip Goodyear	BHP	08-Nov-01	6-May-05	TSR: Relative, sliding scale	53,600	$193,496	$885,472	4.58
Rod Pearse	BLD	06-Nov-01	30-Aug-05	TSR: Relative, sliding scale	700,000	$405,300[i]	$2,569,000	6.34
Rod Pearse	BLD	04-Nov-02	23-Feb-06	TSR: Relative, sliding scale	700,000	$646,800[ii]	$3,073,000	4.75
Kirby Adams	BSL	30-Sep-02	5-Oct-05	TSR: Relative, sliding scale	490,500	$480,690	$4,380,165	9.11
Terry Davis	CCL	24-Apr-02	22-Aug-05	Share price target	200,000	$317,000[iii]	$450,000	1.42
John Fletcher	CML	01-Sep-01	13-Oct-05	TSR/EPS	1,000,000	$920,000[iv]	$3,490,000	3.79
Mike Hawker	IAG	13-Dec-01	26-Aug-05	TSR: Relative, sliding scale	60,000	$58,200	$333,000	5.72

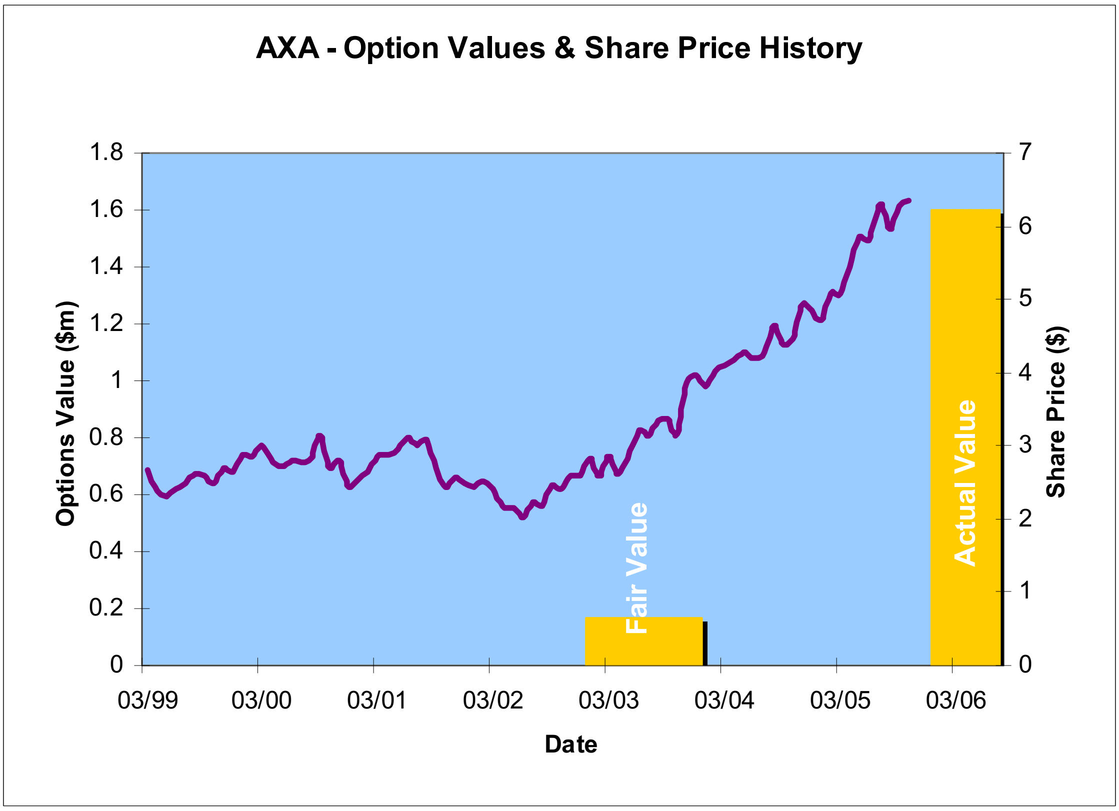
CEO	Co.	Granted	Exercised	Hurdle Type	No. exercised	Total Fair Value (FV)	Realised Value (RV)	RV/FV
Mike Hawker	IAG	23-Nov-02	24-Feb-06	TSR: Relative, sliding scale	168,000	$314,160	$903,840	2.88
Wal King	LEI	27-Mar-02	15-Sep-05	TSR: Outperform index	100,000	$120,000[v]	$324,000	2.70
Wal King	LEI	27-Mar-02	11-Nov-05	TSR: Outperform index	100,000	$120,000[vi]	$449,000	3.74
Wal King	LEI	27-Mar-02	20-Feb-06	TSR: Outperform index	400,000	$480,000[vii]	$2,616,000	5.45
Stuart James	MAY	01-Nov-02	18-Nov-05	EPS/vested on discretion	140,000	$415,800	$830,200	2.00
Stuart James	MAY	01-Aug-03	18-Nov-05	EPS/vested on discretion	140,000	$530,600	$830,200	1.56
Allan Moss	MBL	02-Aug-00	23-May-05	Relative ROE	50,000	$336,000	$1,298,500	3.86
Allan Moss	MBL	02-Aug-01	22-Nov-05	Relative ROE	41,000	$422,300	$1,412,794	3.35
Allan Moss	MBL	02-Aug-01	23-Nov-05	Relative ROE	42,000	$432,600	$1,445,102	3.34
Allan Moss	MBL	02-Aug-01	24-Nov-05	Relative ROE	43,000	$442,900	$1,454,780	3.28
Andrew Reitzer	MTS	14-Dec-01	30-Jan-06	EPS	340,000	$377,400[viii]	$1,106,360	2.93
Mike Wilkins	PMN		28-Feb-06	TSR/ROE	283,333	$510,000	$1,544,164	3.03
Chris Corrigan	PRK	04-Feb-03	8-Dec-05	Retention/ share price[ix]	3,000,000	$1,740,000	$7,930,000	4.56
Geoff Dixon	QAN	24-Nov-00	15-Feb-06	TSR: Unspecified index	173,266	$1,116,954	$701,727	0.63
Geoff Dixon	QAN	17-Oct-02	3-Jan-06	Retention	27,777	$70,366	$113,052	1.61
Frank O'Halloran	QBE	10-Apr-03	10-Apr-06	Retention	110,884	$192,040[x]	$1,673,461	8.71
Frank O'Halloran	QBE	10-Apr-03	10-Apr-06	Retention	47,900	$221,298[xi]	$1,108,022	5.01
Gail Kelly	SGB	12-Dec-01	07-Nov-05	EPS	250,000	$625,000	$2,757,500	4.41
Jeremy Sutcliffe	SGM	28-Feb-02	1 July - 7 July 2005	TSR: Relative, sliding scale	193,798	$269,380	$1,462,690	5.43
John Ellice-Flint	STO	26-Aug-00	02-Sep-05	Absolute TSR	1,000,000	$750,000	$5,690,000	7.59
Matthew Slatter	TAH	08-Oct-02	08-Sep-05	TSR: vesting below median	1,000,000	$929,928[xii]	$3,780,000	4.06
Kim Edwards	TCL	23-Oct-01	22-Sep-05	TSR: Vesting below median	250,000	$122,750	$720,000	5.87
Kim Edwards	TCL	23-Oct-01	14-Dec-05	TSR: vesting below median	250,000	$122,750	$541,450	4.41

CEO	Co.	Granted	Exercised	Hurdle Type	No. exercised	Total Fair Value (FV)	Realised Value (RV)	RV/FV
Kim Edwards	TCL	23-Oct-01	20-Jun-06	TSR: vesting below median	1,000,000	$491,000	$2,575,800	5.25
David Morgan	WBC	01-Mar-02	10-Jun-05	TSR: Relative, sliding scale	200,000	$474,000	$580,000	1.22
David Morgan	WBC	01-Mar-02	10-Jun-05	TSR: Relative, sliding scale	275,000	$651,750	$753,500	1.16
David Morgan	WBC	01-Mar-02	10-Jun-05	TSR: Relative, sliding scale	75,000	$177,750	$234,750	1.32
David Morgan	WBC	04-Mar-03	30-May-06	TSR: Relative, sliding scale	677,886	$1,552,358	$6,460,253	4.16

Appendix 2 - Lapsed Incentives

CEO	Co.	Granted	Lapsed	No. lapsed	Total Fair Value Lapsed	Type of hurdle
Russell Jones	AMC	18-Aug-00	6-Dec-04	1,000,000[xiii]	$457,800	TSR/board discretion
Russell Jones	AMC	18-Aug-00	6-Dec-04	1,000,000[xiv]	$457,800	TSR/board discretion
Russell Jones	AMC	18-Aug-00	6-Dec-04	1,000,000[xv]	$457,800	TSR/board discretion
Russell Jones	AMC	14-Aug-02	6-Dec-04	1,000,000	$1,678,393	TSR: Relative, sliding scale
Russell Jones	AMC	14-Aug-02	6-Dec-04	1,000,000	$1,678,393	TSR: Relative, sliding scale
Russell Jones	AMC	14-Aug-02	6-Dec-04	1,000,000	$1,678,393	TSR: Relative, sliding scale
Andrew Mohl	AMP	25-Nov-02	7-Sep-05	92,278	$459,544	TSR: Relative, sliding scale
Andrew Mohl	AMP	18-Mar-04	7-Sep-05	20,809	$8,531	TSR: Relative, sliding scale
Andrew Mohl	AMP	30-Jun-00	7-Sep-05	250,000	$592,500	TSR: Relative, sliding scale
John Marlay	AWC	26-Mar-03	3-May-05	17,513	$43,607	TSR: Relative, sliding scale
John Marlay	AWC	1-Mar-03	1-Mar-06	24,450	$60,880	TSR: Relative, sliding scale
Chip Goodyear	BHP	1-Oct-01	1-Oct-04	13,657	$99,013	TSR: Relative, sliding scale
Trevor O'Hoy	FGL	1-Sep-01	31-Aug-04	148,000	$321,160	TSR: Relative, sliding scale
Stuart James	MAY	12-Nov-02	30-Jun-05	140,000	$190,400	EPS
Tony Palmer	NCM	8-Nov-01	1-Mar-05	375,000	$375,000	Development of Telfer
Tony Palmer	NCM	6-Feb-03	1-Mar-05	125,000	$257,500	Development of Telfer
Owen Hegarty	OXR	6-Apr-04	1-Jun-06	2,000,000	$205,344	TSR: Relative, sliding scale
Geoff Dixon	QAN	24-Nov-00	1-Jul-05	244,995	$218,045	TSR: Relative, sliding scale
Ziggy Switkowski	TLS	6-Sep-01	06-Dec-04	129,000	$300,570	TSR: Relative, sliding scale
Ziggy Switkowski	TLS	13-Sep-99	13-Sep-04	50,000	$282,000	TSR: Outperform index
Ziggy Switkowski	TLS	13-Sep-99	13-Sep-04	300,000	$414,000	TSR: Outperform index
Ziggy Switkowski	TLS	6-Sep-01	6-Dec-04	1,346,000	$737,760	TSR: Relative, sliding scale
David Morgan	WBC	4-Mar-03	17-Mar-06	422,114	$966,641	TSR: Relative, sliding scale
David Morgan	WBC	1-Mar-02	4-Mar-05	550,000	$1,303,500	TSR: Relative, sliding scale

Appendix 3


AXA - Option Values & Share Price History
Options Value ($m)
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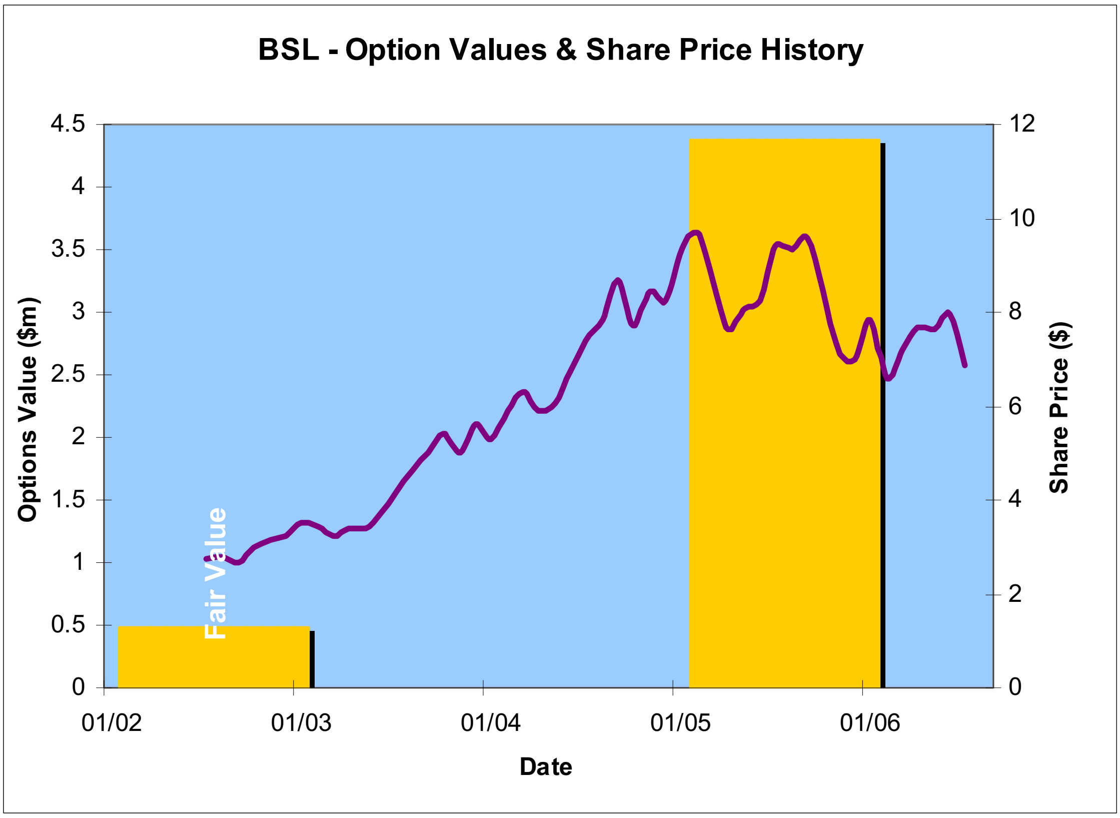
1.4
1.2
1
0.8
0.6
0.4
0.2
0
Share Price ($)
7
6
5
4
3
2
1
0
Fair Value
Actual Value
03/99
03/00
03/01
03/02
03/03
03/04
03/05
03/06
Date


BSL - Option Values & Share Price History
Options Value ($m)
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4
3.5
3
2.5
2
1.5
1
0.5
0
Share Price ($)
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10
8
6
4
2
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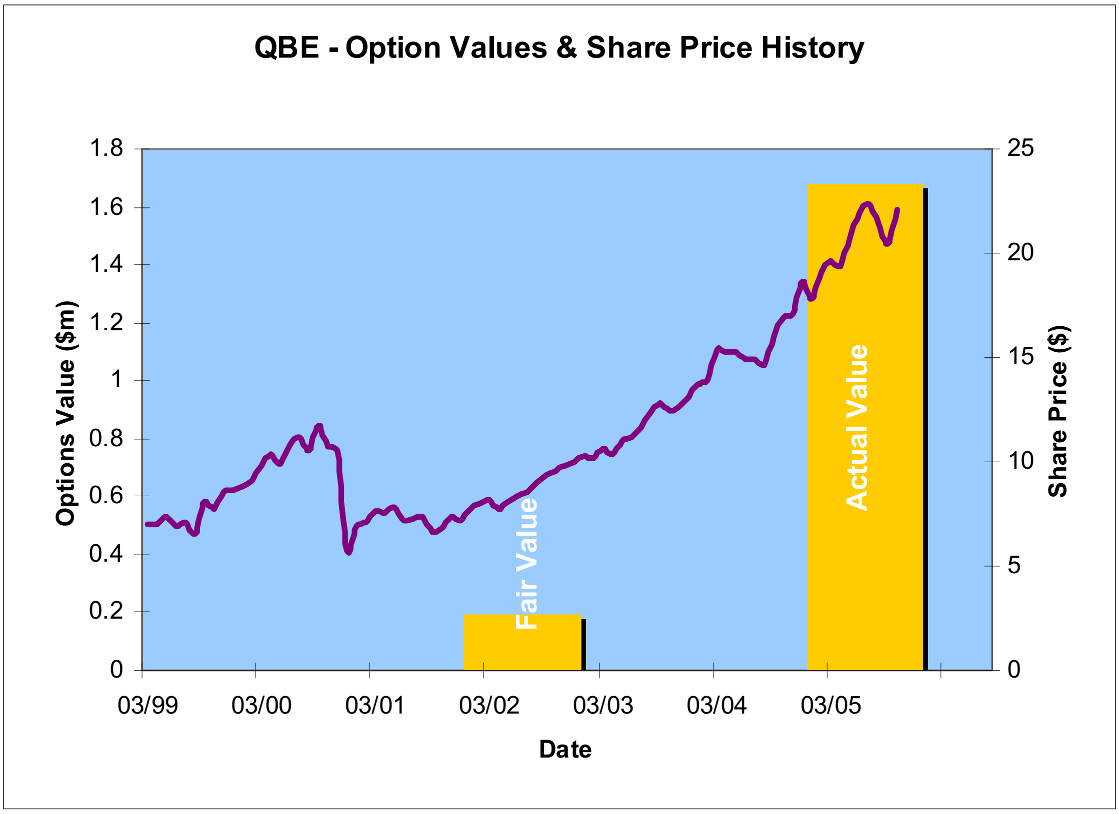
Fair Value
01/02
01/03
01/04
01/05
01/06
Date


QBE - Option Values & Share Price History
Options Value ($m)
Share Price ($)
Date
Fair Value
Actual Value
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03/00
03/01
03/02
03/03
03/04
03/05
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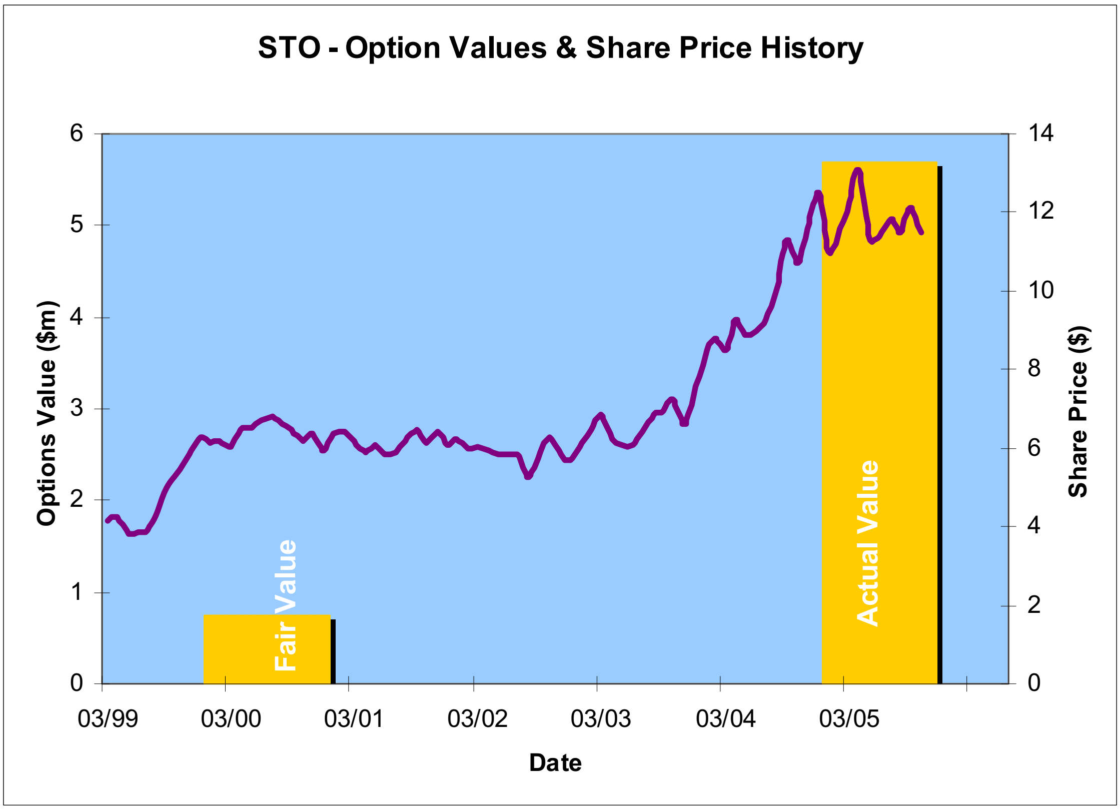
0.4
0.6
0.8
1
1.2
1.4
1.6
1.8
5
10
15
20
25


STO - Option Values & Share Price History
Options Value ($m)
Share Price ($)
Date
Fair Value
Actual Value
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03/00
03/01
03/02
03/03
03/04
03/05
0
1
2
3
4
5
6
8
10
12
14

NOTES TO TABLES

[i] Based on aggregate fair value disclosed in 2002 annual report.
[ii] Based on aggregate fair value disclosed in 2003 annual report.
[iii] Average fair value of options to named executives in the 2002 annual report.
[iv] Average of value of options granted in 2001/02 to Mr Fletcher.
[v] Based on amortised fair value disclosed in 2003 annual report which relates solely to options with exercise price of $10.96.
[vi] See note v.
[vii] See note v.
[viii] Mid-point of the fair value range in the independent expert's 2005 report on the Metcash Trading scheme of arrangement. Fair valuer assumes no Foodland takeover so as to approximate original grant date scenario.
[ix] The last tranche of 1,000,000 options vested two months early as under the conditions of the options granted to Mr Corrigan, if a takeover bid was announced for Patrick, all options would vest immediately.
[x] Based on aggregate fair value of equity grants disclosed as earned in the 2002 annual report; these were granted at the 2003 AGM. This assumes the aggregate fair value of traditional options and zero exercise price options is equal. ISS notes that in the 2005 Annual Report, QBE discloses that the split in value between the two types of instruments granted is 60% performance rights and 40% options for 2005. If this is applied to the 2003 grant, then the fair value of rights granted would increase and the fair value of the options would decrease.
[xi] Based on aggregate fair value of equity grants disclosed as earned in the 2002 annual report; these were granted at the 2003 AGM. This assumes the aggregate fair value of traditional options and zero exercise price options is equal. ISS notes that in the 2005 Annual Report, QBE discloses that the split in value between the two types of instruments granted is 60% performance rights and 40% options for 2005. If this is applied to the 2003 grant, then the fair value of rights granted would increase and the fair value of the options would decrease. The value of performance rights was calculated as being on the maximum number granted at the 2003 AGM; the fair value of performance rights disclosed above is higher as it includes the value of performance rights actually exercised, which includes adjustments to the original number of rights granted to reflect dividends on shares.
[xii] Based on fair value disclosed in 2003 annual report relating to this tranche of options.
[xiii] This tranche of options had actually vested but the options were cancelled by the board. If the options had been exercised on the last trading day prior to the CEO's contract being terminated, the value of this tranche of options would have been $1.87 million.
[xiv] See note xiii.
[xv] See note xiii.