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April 10, 2006

United States Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549

E-mail address: rule-comments@sec.gov

Attention: Nancy M. Morris, Secretary

Re: File No. S7-03-06, Executive Compensation and Related Party Disclosure, Release Nos. 33-8655, 34-53185; IC-27218.

Ladies and Gentlemen:

The Commission and its staff are to be commended for the excellent work reflected in its proposal to amend its executive compensation disclosure rules.

The proposed rules can, however, be improved in the following three respects:

First, the literature suggests that equity based performance incentives are best measured by calculating the extent to which an executive's wealth increases or decreases in response to a change in the registrant's share price. Although the proposed rules significantly enhance executive compensation disclosure, they fail to provide a simple and clear description of how executive wealth changes as a function of registrant share price. Part I of this comment letter describes a relatively simple tabular presentation that can provide shareholder with this information on a prospective retrospective basis.

Second, the proposed rules suggest that registrants be required to disclose the total compensation for up to three employees who are not executive officers but whose total compensation was greater than that of any named executive officer. Part II of this comment letter suggests that these proposed disclosures are unnecessary, easily avoided, and potentially harmful to the very shareholders that the rule seeks to protect. This provision of the proposed rule should therefore not be adopted.

Third, the proposed rules require that registrants make many significant assumptions in order to quantify the effects of termination and change in control provisions. The proposed rule's reliance on extensive assumptions to be made by registrants will cause non-comparability across registrants, give rise to incentives to make assumptions that minimize the value of termination and change in control provisions, and create substantial difficulty for registrants seeking in good faith to comply with the Commission's proposed disclosure requirements. Part III of this letter suggests that the Commission articulate a set of default assumptions that would be applied by all registrants when quantifying the value of termination and change in control provisions, and that these disclosures be arranged in a tabular format. Registrants should also be encouraged to supplement these disclosures with disclosures based on assumptions that they view as more representative of the circumstances the registrant is likely to encounter in the event of a termination or change in control. The use of these default values will reduce or eliminate the non-comparability that inevitably results when similarly situated registrants make different valuation assumptions. It will also eliminate the incentive to make assumptions that minimize the quantified value of termination and change in control provisions, and will achieve these results while still retaining registrants' ability to make assumptions that they view as more representative of the circumstance likely to apply to termination or change in control situations.

I. Executive Wealth and Registrant Share Price

The economic literature suggests that "a key point in analyzing executive incentives is that an executive's incentives are properly measured by *portfolio* incentives … [and that] one cannot determine whether an executive has an appropriate level of incentive by examining newly granted restricted stock and options compensation in a given year."[1] Therefore, in order "to obtain an appropriate measure of economic incentives" the literature strongly urges that "the computation of a manager's compensation should include changes in the value of the CEO's portfolio of stock and options."[2]

The comments of participants at the Rock Center program "Executive Compensation Disclosure: An Analysis of the SEC's Proposed New Rules" April 3, 2006, echo this conclusion.[3] As Professor Yermack suggested, shareholders need to have a practical means by which they can calculate the effect of stock price changes on executive wealth.[4] As Professor Schipper explained, "[i]ncentives are … a function of the employee's wealth," and it is important to measure the "change in the employee's wealth as a function of changes in the state of the world, and also … as a function of whether the item is realized, close to being realized, newly awarded, [or] far from being realized."[5]

The logic supporting this conclusion is rather straightforward. Suppose a CEO has already received option grants for 20 million shares at a strike price well below the issuer's current market price and that these options have vested. If the board grants additional options for 1

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[1] John E. Core, Wayne R. Guay, and David F. Larcker, Executive Compensation and Incentives. Federal Reserve Bank of New York Economic Policy Review 27, 30 (April 2003) (emphasis in original) (citations omitted).
[2] John E. Core, Wayne R. Guay, and Robert E. Verrecchia, Price versus Non-Price Performance Measures in Optimal CEO Compensation Contracts, 78 Accounting Rev. 957, 962 (2003).
[3] The transcript of this program has been separately filed as a comment in this proceeding and is cited hereinafter as "Rock Center Proceedings."
[4] Rock Center Proceedings at 18 – 20.
[5] Rock Center Proceedings at 34.

million shares at market, those options may have material value but they would still constitute a small percentage of the equity related incentive facing the CEO. Instead, this CEO's incentives would be driven primarily by the value of the vested options rather than by the estimated value of the new option package. A singular focus on the grant date value of the most recent option (however measured) will therefore dramatically misstate the true incentive effects facing the CEO and the issuer.

Put another way, it is important to know how much "skin" the executive has in the game and the extent to which the executive's incentives are aligned with shareholders. Does the executive's portfolio holdings combined with his compensation arrangements create a situation in which the shareholders and the executive share and share alike in the event the registrant's share price rises or falls, or does the executive face incentives that differ materially from those faced by the corporation's shareholders?

The economic literature further suggests that "[o]ption compensation makes CEO wealth a convex function of stock price. Consequently, the CEO benefits from an increase in the stock price associated with aggressive accounting. However, the loss to CEO wealth in the event of a decline in stock price is limited. Management is rewarded in good times but not penalized as much in bad times…. The evidence is consistent with the hypothesis that incentives from options [because of their convexity] encourage aggressive accounting practices that result in a restatement." [6] In contrast, there appears to be no evidence that "incentives from equity and restricted stock [holdings] are associated with misreporting" because those forms of equity exposure "expose the CEO to price declines and therefore [may not generate] a higher propensity to misreport."[7]

The implication of this strand of the literature is that shareholders rationally have an interest in measuring the extent to which a CEO's total portfolio exposure to the issuer's stock price displays the sort of convexity - - i.e., tendency to rise sharply with the issuer's stock price, but not to fall proportionately with the issuer's stock price declines - - that might be associated with an incentive to engage in aggressive accounting practices. Again, a singular focus on the grant date valuation of the most recent option grants will not adequately describe this exposure.

Shareholders and boards are also aware that "the challenge in designing multi-year option plans is to create sufficient upside potential for incentive alignment purposes while at the same time preserving the company's ability to retain and motivate executives if the stock price falls sharply."[8] For this reason, shareholders would have a reason to be interested in the extent to which an executive's holdings in the issuer provide distinct incentives to generate upside potential and, quite distinctly, to remain motivated if the stock price declines sharply.

The Commission's proposed rules, however, provide no easy mechanism for addressing any of these concerns. In particular, at no point do the proposed rules require a simple and

[6] Natasha Burns and Simi Kedia, The Impact of Performance-Based Compensation on Misreporting, 79 J. Fin. Econ. 35, 36 (2006).
[7] Id. at 37.
[8] Brian J. Hall, Six Challenges in Designing Equity-Based Pay, 15 J. Applied Corp. Fin. 21, 28 (2003).

straightforward description of how changes in issuer stock price might affect the value of senior executive holdings, or how such changes might implicate the retention value of existing pay packages. Nor do the rules propose the disclosure of information in a format that would readily allow shareholders to perform such calculations on their own.

There are two potential approaches to solving this problem. The first, as described by Professor Yermack at the Rock Center conference, would be to incorporate a British style requirement that would mandate the disclosure of grant date and other information sufficient to allow certain knowledgeable users to calculate the wealth effects of outstanding grants.[9] An example of British style disclosure, as distributed by Professor Yermack at the Rock Center Conference, is attached as Exhibit A.

To be fully effective, however, these requirements would also have to call for a consistent form of reporting actual holdings, vested exercised and unexercised options, vested and unvested restricted stock grants, offsetting hedge positions and pledges, and any cash grants that would be linked to stock price performance. In the interests of brevity, I describe this approach as "expanded British-style disclosure."

While this approach would offer scholars, consultants, and other observers who are expert in option valuation with all the data necessary to conduct the necessary calculations, the average shareholder would remain in the dark about the extent to which executive wealth would be a function of changes in shareholder price. The second approach, described below, addresses this problem and is described as "direct wealth effect disclosure."

Direct wealth effect disclosure would, in effect, require that registrants gather all the information required for expanded British-style disclosure, and conduct the computations necessary to estimate the wealth effects of prospective stock price changes in a manner consistent with the technique used to calculate grant date valuations in accordance with 123-R. The disclosures filed with the Commission would then describe the output of these calculations. These calculations could provide estimates of the extent to which each named executive officer's wealth would increase or decrease in the future as a result of changes in the registrant's share price. The calculations would take into account all of the executive's equity holdings, options grants, restricted stock, pledges, hedged positions, and other compensation that is a function of changes in share price. These calculations could be presented in the aggregate and separately for: (a) equity that is owned and vested, as distinguished from (b) equity that is unvested. Table 1 describes one possible format for such disclosures.

[9] Rock Center Proceedings at 18 -19.

TABLE 1
Sensitivity of Executive Wealth to Prospective Changes in Issuer Share Price

Change in Value of Equity and Synthetic Equity in the Event of a:	Name and Principal Position				
	PEO	O	A	B	C
10% increase in share price [1]					
20% increase in share price [2]					
30% increase in share price [3]					
50% increase in share price [4]					
10% decrease in share price [5]					
20% decrease in share price [6]					
30% decrease in share price [7]					
50% decrease in share price [8]					
Change in Value of Owned and Vested Equity and Synthetic Equity in the Event of a:					
10% increase in share price [9]					
20% increase in share price [10]					
30% increase in share price [11]					
50% increase in share price [12]					
10% decrease in share price [13]					
20% decrease in share price [14]					
30% decrease in share price [15]					
50% decrease in share price [16]					
Change in Value of Unvested Equity and Synthetic Equity in the Event of a:					
10% increase in share price [17]					
20% increase in share price [18]					
30% increase in share price [19]					
50% increase in share price [20]					

10% decrease in share price [21]					
20% decrease in share price [22]					
30% decrease in share price [23]					
50% decrease in share price [24]					
Note 1: Line 1 = Line 9 + Line 17; Line 2 = Line 10 + Line 18; Line 3 = Line 11 + Line 19; Line 4 = Line 12 + Line 20; Line 5 = Line 13 + Line 21; Line 6 = Line 14 + Line 22; Line 7 = Line 15 + Line 23; Line 8 = Line 16 + Line 24.					

Proposed Table 1 would address this concern at two levels of detail, and to achieve this result is divided into three distinct parts. The top part describes the aggregate change in value of the executives' total holdings in the issuer as a consequence of predefined changes in the value of the issuer's shares. The instructions to the table would provide that all of the executives' holdings, actual and potential, real or synthetic, be included in the computation. Actual equity holdings, restricted stock, options and other types of equity related exposure would all be included and aggregated in the table's data. Options or other interests that are "out of the money" at any price point would be valued using the same technique applied to value the executives' at the money option grants. The issuer would also assume that grants that are contingent on performance or on time based vesting would all be issued because the conditions to vesting will be satisfied.

The top portion of Proposed Table 1 would thereby provide a straightforward description of the extent to which the registrant's senior executives' compensation increases or decreases as a function of changes in the registrant's stock price, and thereby offer a more direct description of the true incentive effect of stock price changes on changes in executive wealth.

The second and third portions of Table 1 are designed to disaggregate executive compensation into two distinct components: (a) compensation that has not as yet vested and (b) shares that are held outright by the executives or option grants that have already vested. To the extent that an executive holds shares that have not as yet vested, either because performance targets have not yet been attained or because they have not satisfied time of service requirements, the value of those grants measures the economic benefit that the executive would have to walk away from in the event the executive left the registrant to join another firm, or for any other reason. Those values therefore measure a portion of the "retention power" of the executive's pay package and are measured separately in the second part of Proposed Table 1.

Shares that are owned outright or grants that have already vested do not have equivalent retention power because the approximate values would be kept by the executives even if they retired immediately from the registrant's employ,[10] and are valued separately in the third portion of Proposed Table 1.

[10] I describe these values as "approximate" because option grants often require that the recipient exercise any vested grants within a specific period of termination, say 90 days. This requirement reduces the value of the optionality in the compensation package and causes option grants to be valued at their intrinsic values rather than at their option values. In order to avoid the need for making arbitrary assumptions as to when or whether

Direct wealth effect disclosure and expanded British style disclosure are complementary forms of disclosure that are not mutually exclusive. Compensation experts might prefer expanded British style disclosure because they would then be able to apply their own valuation models in order to estimate the wealth effects of changes in registrant share price. Shareholders who lack the ability to conduct these computations might, on the other hand, prefer direct wealth effect disclosure because they would otherwise lack the ability to make any sense of the implications of expanded British style disclosure. Both constituencies can, however, be satisfied if the Commission mandates direct wealth effect disclosure as part of the proxy statement, and calls for registrants to provide supplemental expanded British style disclosure that would be considered furnished but not filed and that would be made available only in machine readable form.

At first glance, either of these approaches might seem objectionable because they appear to impose an overwhelming information gathering requirement on all registrants, i.e., registrants would be required to have a detailed, consistent, and organized method of maintaining a data base that documents all equity related compensation and its terms and conditions, and would then have to apply a competent methodology for estimating the potential value for those grants. There would also be the threat of drowning shareholders with a mass of complicated data. Both of these complaints are, however, easily overstated and resolved.

First, it is difficult to comprehend how a compensation committee can determine the incentive effects of its compensation policy unless it already has the ability to conduct calculations of the sort contemplated by Table 1. Indeed, any registrant that relies on a competently constructed tally sheet already has the information required to comply with expanded British style disclosure, or something very close to it, and all that need be done is the application of the same option valuation technique applied pursuant to 123R. Registrants who do not have such tally sheets would incur one-time costs in establishing those databases, but the continuing maintenance costs for operating those databases would be relatively low. Thus, to the extent that a direct wealth effect disclosure requirement causes some registrants to incur additional costs because they have to build databases that can track the wealth effects of the equity-based compensation offered to their senior executives, the requirement will, I believe, add substantial value to compensation setting process. It will make transparent to all parties involved the extent to which executive and shareholder interests are or are not aligned, and the magnitude of the potential wealth gains and losses to which the executives are exposed.

Second, the form of disclosure described in proposed Table 1 is calculated to minimize the flood of data that might otherwise overwhelm the disclosure process by summarizing the wealth implications of changes in share price without providing extensive detail on the computations underlying those disclosures. As already suggested, that additional detail can be contained in additional XBRL tagged data that would be provided as a supplement to the filing and that would be of interest primarily to professionals and academics.

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vesting conditions are satisfied, it would be simpler to complete Proposed Table 1 on the assumption that all unvested grants will eventually become vested on the earliest possible date. This approach provides for a “best case” estimate of the retention value of unvested equity grants.

II. Disclosure of Compensation of Non-Executive Employees.

The proposed rules call for "an additional item that would require disclosure for up to three employees who were not executive officers during the last completed fiscal year and whose total compensation for the last completed fiscal year was greater than that of any of the named executive officers." 71 Fed. Reg. at 6558. These proposed disclosures are unnecessary, can harm shareholder interests, and can be easily avoided. They should therefore be abandoned.

The dominant concern that animates the call for broader compensation disclosure is the observation that boards of directors may be subject to a variety of agency problems that cause them either to set executive compensation too high or to fail to tie compensation appropriately to executive or corporate performance. There is no apparent concern of which I am aware in the academic literature or in the general press that an equivalent problem exists with regard to the compensation of non-executive employees. Moreover, to the extent that non-executive employees are even more highly paid than executive employees, it is generally reasonable to assume that the lower-paid executives are driven to approve these higher pay packages by competitive market forces. Indeed, the general press has observed that the disclosure requirement as currently drafted will call for the disclosure of compensation paid to athletes, actors, portfolio fund managers, physicians, and commission salespersons. It is hard to appreciate the existence of a governance or market failure in any of these labor markets that rationally supports disclosure of the sort contemplated by the proposed rules.

Further, if a registrant and employer wish legally to avoid application of the proposed disclosure requirements, they will often be able to restructure the employment arrangement so that the former employer enters a contract or consulting arrangement with a personal services company owned by the former employee, or with the employee acting as a sole proprietor. This arrangement can successfully avoid the disclosure requirement because the proposed rule does not apply to contractor relationships - - it only implicates employees. This alternative arrangement could, however, be more expensive and inefficient for the employer and employee alike because of the transactions and other costs involved in establishing such a relationship. This disclosure rule can therefore generate wasteful avoidance costs by parties who seek legally to avoid its application.

The proposed rule also runs the risk of harming the very shareholders that it is designed to protect. Although the proposed rule does not call for disclosure of the names of the three additional highly paid employees, the Commission should not be fooled into thinking that the names of these employees will remain a secret. Fellow employees will scrutinize the disclosures with a gimlet eye and will often be able to deduce precisely who got paid what. Just about every employee knows the identity of a company's top salespeople and traders, but few know exactly how much they make. The proposed rules will solve that mystery, not only for fellow employees, but also for competitors. Fellow employees who feel that they are undervalued relative to compensation paid to the "top three" could agitate for raises and would be armed in these negotiations with data that they otherwise would not have. It is hard to see how this form of wage escalation benefits shareholders.

Moreover, highly paid employees who value their privacy, and for whom alternative contractual arrangements are inefficient or infeasible, could decide to work for competitors that are not publicly traded and where no such disclosure obligations apply. Thus, a successful proprietary trader at a publicly held investment bank might decide that rather than have his pay package plastered all over the Wall Street Journal for everyone to see, that he might just as well leave the bank and either form his own hedge fund or work for a well-capitalized, privately held competitor. In either event, the bank's shareholders would be harmed, not helped.

III. Termination and Change in Control Provisions.

The proposed rules call for "narrative disclosure of … information regarding termination and change in control provisions" as well as "quantitative disclosure … even where uncertainties exist as to amounts payable under these plans and arrangements." 71 Fed. Reg. at 6562 – 63. The Proposing Release further provides that "[i]f uncertainties exist as to the provision of payments or benefits or as to the amounts involved, the company is required to make reasonable estimates and to disclose material assumptions underlying its estimates." Id. at 6563.

Prominent law firms, have, however, complained of several problems that arise in connection with the estimates that must be made in order to provide for such quantitative disclosures. One firm observes that:

"[S]uch estimates and assumptions may be particularly problematic in connection with change-in-control payments, especially when payments to an executive include Section 280G "golden parachute" tax gross-ups. If payments depend on the value of consideration that would be received in a change-in control transaction, it is not clear whether required "reasonable estimates" would permit valuing the transaction at an historical market price of the company's stock (such as the fiscal year-end market price) rather than to predict (and publicly disclose) the amount of a likely change-in-control price. In addition, the assumptions required to determine the 280G tax gross-up (such as whether the change-in-control payments are reasonable compensation for past services and assumptions with respect to the valuation of future restrictions such as non-compete agreements) may later raise issues about the consistency of treatment between future tax positions taken by the company with the IRS and the disclosure made to stockholders in public documents." [11]

Counsel at a second prominent firm similarly observe that:

" Calculation of the golden parachute excise taxes and the related gross-ups is extremely complex and dependent on the particular facts of specific transactions. As a result, the

[11] Simpson Thacher & Bartlett LLP, Analysis of SEC's Proposed New Rules Concerning Executive Compensation and Related Disclosure, March 31, 2006, at A-25 and A-26.

calculation of such amounts would in an annual proxy require a registrant to make a number of uncertain assumptions with respect to, among other things, the dates of an employment termination or proposed transaction, transaction price and type of consideration, treatment of equity compensation awards in the transaction, valuation of equity compensation for purposes of the excise tax, valuation of restrictive covenants and potentially complex future tax positions of the executives."[12]

The need for extensive assumptions in connection with the provision of the suggested quantitative disclosures gives rise to three distinct problems. First, registrants acting in good faith will find it authentically difficult to make estimates as to many of the inputs required to generate the necessary assumptions. They will have a legitimate concern that, by making the necessary assumptions, they are somehow endorsing estimates as to which they have little or no confidence. Second, there will be a natural tendency among some registrants to make assumptions that minimize the magnitude of the disclosures required by the proposed rule. As an example of this behavior, consider historic practice with regard to the assumptions necessary to calculate pension and other post-retirement obligations. There is a clear history that these assumptions have been "modulated" so as to minimize the magnitude of the projected liabilities, and the same forces will likely be at work in connection with the proposed disclosures. Third, as currently structured, the proposal will generate fundamentally non-comparable disclosures. Consider the situation of two registrants with identical termination and change in control provisions. If those firms adopt different assumptions they can generate quite different disclosures, and users will then be left to their own devices to tease out the extent to which differences in disclosure reflect differences in the terms and conditions of employment agreements of differences in the assumptions and valuation methodologies applied to quantify the effects of those agreements.

All of these problems can be addressed if the Commission provides default values to be applied in the quantification of termination and change in control provisions, and also permits issuers to provide additional disclosures applying any other assumptions that the registrant deems more representative of the facts and circumstances likely to apply in the event of a termination or change in control.

The default assumptions for termination provisions might, for example, require a calculation of the payout that would result in the event of a termination as of the last trading day of the most recently concluded fiscal year, on the assumption that the highest relevant marginal federal, state, and local tax rates would be applied to any relevant gross up provisions. This approach minimizes the need for registrants to rely on hypothetical scenarios and provides an objective, quantifiable benchmark for the application of the Commission's proposed new disclosure standards.

The default assumption for change in control provisions might, for example, require the calculation of the payout that would result in the event of an acquisition being triggered as of the last trading day of the most recent fiscal year at a hypothetical premium of 25% to the trailing 30 day average stock price, in an all-cash transaction, on the assumption that the

[12] Adam Chinn, et al., Change-in-Control and Termination-Related Disclosure: A Changing Landscape, Wachtell, Lipton, Rosen & Katz, January 30, 2006, at 2.

highest relevant marginal federal, state, and local tax rates would be applied to any relevant gross up provisions.

No doubt, this proposal to provide these default values has its own meaningful flaws. The default values will be entirely inappropriate for some registrants who are subject to market forces quite different from those that drive the assumptions underlying the default values. For example, some registrants are more likely to engage in merger of equals transactions that convey no premium, while other registrants are more likely to be acquired at multiples far above those suggested in the default values. To address this obviously reasonable criticism, registrants should be encouraged to provide alternative valuations that reflect alternative, more reasonable assumptions. Further, registrants who wish to avoid dramatic disclosures that might be required under the Commission's proposed default values could attempt to draft contracts that would cause higher payouts only under terms and conditions that are not captured by any of the default values that might ultimately be adopted. In order to address this concern, the Commission's rules should require textual description of such terms and conditions.

Conclusion.

The proposed rules constitute a significant and beneficial advance in the state of the art of corporate disclosure. They can, however, be improved if they are expanded to provide for accessible disclosure of the prospective wealth effects of changes in registrant share price, if the requirement for disclosure of compensation paid to certain non-executive officers is deleted, and if they are amended to provide for default assumptions to be applied to the quantification of termination payments and change in control provisions.

Respectfully submitted,

Joseph A. Grundfest

Compensation Disclosure
Best Practices:

Executive Stock Option Holdings
as done by companies in the U.K.

Examples:

BP (British Petroleum)

Cadbury Schweppes

Royal Bank of Scotland Group

- *Full inventory* of each executive's options is shown, including award date, vesting date, expiration date, and exercise price *of each award*.
- This detail is necessary for correct calculation of option values and incentive measures such as "delta" and "vega."
- U.S. disclosure is especially inadequate when options are out-of-the-money.

SHARE OPTIONS

	Option type	At 1 Jan 2005	Granted	Exercised	At 31 Dec 2005	Option price	Market price at date of exercise	Date from which first exercisable	Expiry date
Lord Browne	SAYE	4,550	–	–	4,550	£3.50		1 Sep 2008	28 Feb 2009
	EDIP	408,522	–	–	408,522	£5.99		15 May 2001	15 May 2007
	EDIP	1,269,843	–	–	1,269,843	£5.67		19 Feb 2002	19 Feb 2008
	EDIP	1,348,032	–	–	1,348,032	£5.72		18 Feb 2003	18 Feb 2009
	EDIP	1,348,032	–	–	1,348,032	£3.88		17 Feb 2004	17 Feb 2010
	EDIP	1,500,000	–	–	1,500,000	£4.22		25 Feb 2005	25 Feb 2011
Dr D C Allen	EXEC	37,000	–	–	37,000	£5.99		15 May 2003	15 May 2010
	EXEC	87,950	–	–	87,950	£5.67		23 Feb 2004	23 Feb 2011
	EXEC	175,000	–	–	175,000	£5.72		18 Feb 2005	18 Feb 2012
	EDIP	220,000	–	–	220,000	£3.88		17 Feb 2004	17 Feb 2010
	EDIP	275,000	–	–	275,000	£4.22		25 Feb 2005	25 Feb 2011
I C Conn	SAYE	1,355	–	1,355	0	£4.98	£6.38	1 Sep 2005	28 Feb 2006
	SAYE	1,456	–	–	1,456	£3.50		1 Sep 2008	28 Feb 2009
	SAYE	1,186	–	–	1,186	£3.86		1 Sep 2009	28 Feb 2010
	SAYE	0	1,498	–	1498	£4.41		1 Sep 2010	28 Feb 2011
	EXEC	72,250	–	–	72,250	£5.67		23 Feb 2004	23 Feb 2011
	EXEC	130,000	–	–	130,000	£5.72		18 Feb 2005	18 Feb 2012
	EXEC	160,000	–	–	160,000	£3.88		17 Feb 2006	17 Feb 2013
	EXEC	126,000	–	–	126,000	£4.22		25 Feb 2007	25 Feb 2014
Dr B E Grote[a]	SAR	35,200	–	–	35,200	$25.27		6 Mar 1999	6 Mar 2006
	SAR	40,000	–	–	40,000	$33.34		28 Feb 2000	28 Feb 2007
	BPA	10,404	–	–	10,404	$53.90		15 Mar 2000	14 Mar 2009
	BPA	12,600	–	–	12,600	$48.94		28 Mar 2001	27 Mar 2010
	EDIP	40,182	–	–	40,182	$49.65		19 Feb 2002	19 Feb 2008
	EDIP	58,173	–	–	58,173	$48.82		18 Feb 2003	18 Feb 2009
	EDIP	58,173	–	–	58,173	$37.76		17 Feb 2004	17 Feb 2010
	EDIP	58,333	–	–	58,333	$48.53		25 Feb 2005	25 Feb 2011
Dr A B Hayward	SAYE	3,302	–	–	3,302	£5.11		1 Sep 2006	28 Feb 2007
	EXEC	34,000	–	–	34,000	£5.99		15 May 2003	15 May 2010
	EXEC	77,400	–	–	77,400	£5.67		23 Feb 2004	23 Feb 2011
	EXEC	160,000	–	–	160,000	£5.72		18 Feb 2005	18 Feb 2012
	EDIP	220,000	–	–	220,000	£3.88		17 Feb 2004	17 Feb 2010
	EDIP	275,000	–	–	275,000	£4.22		25 Feb 2005	25 Feb 2011
J A Manzoni	SAYE	878	–	–	878	£4.52		1 Sep 2007	28 Feb 2008
	SAYE	2,548	–	–	2,548	£3.50		1 Sep 2008	28 Feb 2009
	SAYE	847	–	–	847	£3.86		1 Sep 2009	28 Feb 2010
	EXEC	12,000	–	12,000	0	£2.04	£5.52	28 Feb 1998	28 Feb 2005
	EXEC	34,000	–	–	34,000	£5.99		15 May 2003	15 May 2010
	EXEC	72,250	–	–	72,250	£5.67		23 Feb 2004	23 Feb 2011
	EXEC	175,000	–	–	175,000	£5.72		18 Feb 2005	18 Feb 2012
	EDIP	220,000	–	–	220,000	£3.88		17 Feb 2004	17 Feb 2010
	EDIP	275,000	–	–	275,000	£4.22		25 Feb 2005	25 Feb 2011

The closing market prices of an ordinary share and of an ADS on 31 December 2005 were £6.19 and $64.22 respectively.
During 2005, the highest market prices were £6.84 and $72.27 respectively and the lowest market prices were £5.04 and $56.61 respectively.

EDIP = Executive Directors' Incentive Plan adopted by shareholders in April 2005 as described on pages 165-167.
BPA = BP Amoco share option plan, which applied to US executive directors prior to the adoption of the EDIP.
SAR = Stock Appreciation Rights under BP America Inc. Share Appreciation Plan.
SAYE = Save As You Earn employee share scheme.
EXEC = Executive Share Option Scheme. These options were granted to the relevant individuals prior to their appointments as directors and are not subject to performance conditions.

[a] Numbers shown are ADSs under option. One ADS is equivalent to six ordinary shares.

Directors' and CEC members' Share Options over ordinary shares of 12.5p each (table seven)

Name of Director and Scheme	As at 29 Dec 2003 (or date of appointment if later)	Granted	Exercised (lapsed)	As at 2 Jan 2005 (or date of resignation if earlier)	Exercise Price £	Market price at exercise date £	Gain made on exercise £ (k)	Exercisable From	To
Ken Hanna (a)									
(c)	125,000	–	–	125,000	4.2475			27 Mar 2007	26 Mar 2014
(d)	–	205,000	–	205,000	4.395			28 Aug 2007	27 Aug 2014
(e)	–	4,699	–	4,699	3.5160			1 Feb 2010	31 Jul 2010
	125,000	209,699	–	334,699					
David Kappler (b)									
(c)	300,000	–	–	300,000	4.09			2 Sep 2003	2 Sep 2010
(c)	300,000	–	–	300,000	4.77			1 Sep 2004	31 Aug 2011
(c)	300,000	–	–	300,000	4.825			24 Aug 2005	23 Aug 2012
(c)	350,000	–	–	350,000	3.515			10 May 2006	9 May 2013
(e)	1,010	–	1,010	–	3.414	4.17	764	1 Jan 2004	30 Jun 2004
	1,251,010	–	1,010	1,250,000			764		
Bob Stack									
(c)	250,000	–	–	250,000	4.09			2 Sep 2003	1 Sep 2010
(c)	250,000	–	–	250,000	4.77			1 Sep 2004	31 Aug 2011
(c)	250,000	–	–	250,000	4.825			24 Aug 2005	23 Aug 2012
(c)	350,000	–	–	350,000	3.515			10 May 2006	9 May 2013
(c)	49,978	–	49,978	–	2.0457	4.64	130,782	2 Nov 1997	1 Nov 2004
(c)	54,000	–	–	54,000	2.425			28 Sep 1998	27 Sep 2005
(c)	90,000	–	–	90,000	2.595			28 Sep 1999	27 Sep 2006
(d)	–	177,000	–	177,000	4.395			28 Aug 2007	27 Aug 2014
(f)	2,096	16	2,112	–	$5.963	4.48	1,602	19 Apr 2004	30 Apr 2004
(f)	2,140	–	–	2,140	$4.665			18 Apr 2005	29 Apr 2005
(f)	–	1,512	–	1,512	$6.613			17 Apr 2006	28 Apr 2006
	1,298,214	178,528	52,090	1,424,652			132,384		
Todd Stitzer									
(c)	275,000	–	–	275,000	4.09			2 Sep 2003	2 Sep 2010
(c)	275,000	–	–	275,000	4.77			1 Sep 2004	31 Aug 2011
(c)	300,000	–	–	300,000	4.825			24 Aug 2005	23 Aug 2012
(c)	500,000	–	–	500,000	3.515			10 May 2006	9 May 2013
(d)	–	327,000	–	327,000	4.395			28 Aug 2007	27 Aug 2014
	1,350,000	327,000	–	1,677,000					
John Sunderland									
(c)	500,000	–	–	500,000	4.09			2 Sep 2003	1 Sep 2010
(c)	500,000	–	–	500,000	4.77			1 Sep 2004	31 Aug 2011
(c)	500,000	–	–	500,000	4.825			24 Aug 2005	23 Aug 2012
(c)	500,000	–	–	500,000	3.515			10 May 2006	9 May 2013
(c)	135,356	–	135,356	–	2.0457	4.42	325,436	2 Nov 1997	1 Nov 2004
(c)	200,000	–	75,000	125,000	2.595	4.66	153,750	28 Sep 1999	27 Sep 2006
(e)	3,117	–	–	3,117	3.248			1 Feb 2006	31 July 2006
	2,338,473	–	210,356	2,128,117			479,186		
CEC members	5,033,474	1,234,538	287,737	5,980,275	4.117	4.71	389,099	28 Sep 1998	27 Aug 2014

Notes
(a) Ken Hanna was appointed as a Director on 13 April 2004.
(b) David Kappler resigned as a Director on 13 April 2004.
(c) Share Option Plan 1994.
(d) Share Option Plan 2004.
(e) Savings-Related Share Option Scheme 1982.
(f) US and Canada Employee Stock Purchase Plan 1994.
(g) No options lapsed during the year.
(h) No payment was made on the granting of any of these options.
(i) Non-Executive Directors are not granted share options.
(j) The market price of an ordinary share on 31 December 2004 (the last dealing day in the financial year) was £4.85. The highest and lowest market prices of an ordinary share in the year were £4.87 and £3.93 respectively.
(k) Where some or all of the shares were sold immediately after the exercise of an option, the gain shown is the actual gain made by the Director or CEC member. If some or all of the shares were retained, the gain is a notional gain calculated using the market price on the date of exercise.

Share options

Options to subscribe for ordinary shares of 25p each in the company granted to, and exercised by, directors during the year to 31 December 2005 are included in the table below:

	Options held at 1 January 2005	Options granted in 2005	Options exercised in 2005 Number	Options exercised in 2005 Market price at date of exercise £	Option price £	Options held at 31 December 2005 Number	Options held at 31 December 2005 Exercise period
Sir George Mathewson	69,257				9.33	69,257	11.05.01 – 10.05.08
	147,247				7.81	147,247	29.03.03 – 28.03.10
	150				12.40	150	09.08.03 – 08.08.06*
	20,100				17.18	20,100	14.08.04 – 13.08.11
	1,347				13.64	1,347	01.10.08 – 31.03.09*
	19,500				18.18	19,500	14.03.05 – 13.03.12
	36,400				12.37	36,400	13.03.06 – 12.03.13
	36,044				17.34	36,044	11.03.07 – 10.03.14
		41,570			17.29	41,570	10.03.08 – 09.03.15
	330,045	41,570				371,615	
Sir Fred Goodwin	164,571				8.75	164,571	07.12.01 – 06.12.08
	2,963				11.18	2,963	04.03.02 – 03.03.09
	27,306				11.97	27,306	03.06.02 – 02.06.09
	153,648				7.81	153,648	29.03.03 – 28.03.10
	43,700				17.18	43,700	14.08.04 – 13.08.11
	1,713		1,713	16.19	9.85	–	
	41,300				18.18	41,300	14.03.05 – 13.03.12
	72,800				12.37	72,800	13.03.06 – 12.03.13
	144,175				17.34	144,175	11.03.07 – 10.03.14
		159,051			17.29	159,051	10.03.08 – 09.03.15
		1,267			13.04	1,267	01.10.10 – 31.03.11*
	652,176	160,318	1,713			810,781	
Mr Fish	107,877				9.33	107,877	11.05.01 – 10.05.08
	150				12.40	150	09.08.03 – 08.08.06*
		37,603			17.29	37,603	10.03.08 – 09.03.15
	108,027	37,603				145,630	
Mr Pell	51,216				7.81	51,216	29.03.03 – 28.03.10
	29,100				17.18	29,100	14.08.04 – 13.08.11
	27,600				18.18	27,600	14.03.05 – 13.03.12
	49,800				12.37	49,800	13.03.06 – 12.03.13
	47,217				17.34	47,217	11.03.07 – 10.03.14
		50,607			17.29	50,607	10.03.08 – 09.03.15
	204,933	50,607				255,540	
Mr Robertson**	56,635				9.33	56,635	11.05.01 – 10.05.08
	82,654				11.18	82,654	04.03.02 – 03.03.09
	128,040				7.81	128,040	29.03.03 – 28.03.10
	36,400				17.18	36,400	14.08.04 – 13.08.11
	303,729					303,729	
Mr Watt***	70,148				12.83	70,148	04.09.03 – 03.09.10
	23,300				17.18	23,300	14.08.04 – 13.08.11
	22,100				18.18	22,100	14.03.05 – 13.03.12
	42,500				12.37	42,500	13.03.06 – 12.03.13
	43,253				17.34	43,253	11.03.07 – 10.03.14
		57,259			17.29	57,259	10.03.08 – 09.03.15
	201,301	57,259				258,560	

* Options held under the sharesave and option 2000 schemes, which are not subject to performance conditions.

** Mr Robertson retired from the Board on 20 April 2005.

*** Mr Watt resigned from the Board on 31 January 2006.

The performance conditions for options granted in 2005 are detailed on page 123.