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If you have sold or otherwise transferred all your shares in Gresham Computing plc please forward this document and the accompanying form of proxy at once to the purchaser or transferee or to the stockbroker, bank or other agent through whom the sale or transfer was effected for onward transmission to the purchaser or transferee.

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# **Gresham Computing plc**

Proposal to establish  
new Executive Option Plan

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**Gresham Computing plc**  
(registered in England and Wales No. 1072032)

Registered office  
Sopwith House  
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21 May 2007

Dear Shareholder

**Proposal to establish a new Executive Option Plan**

Several important changes have taken place at Gresham Computing plc (the **Company** or **Gresham**) in the last few months and, importantly, the management team has been strengthened. To assist in achieving its challenging objectives over the coming years, the Company is proposing to introduce a new executive option plan which aims to strongly align the interests of management with shareholders.

The proposed plan has been designed to reward performance that leads to an increase in shareholder return, measured by performance against absolute share price targets for the Company, over a 3 to 5 (or 6) year period. No reward is proposed for shareholder returns that fall below the target levels of share performance.

The Listing Rules require that shareholder approval be sought for the adoption of any long-term incentive scheme. Accordingly, such approval will be sought at the Company's Annual General Meeting to be held at the offices of KBC Peel Hunt Ltd, 4th Floor, 111 Old Broad Street, London EC2N 1PH on 29 June 2007 at 10.00am. The notice of meeting, including the relevant ordinary resolution to be proposed, is enclosed. The Appendix to this letter contains background information on the proposed new plan and details of its principal terms.

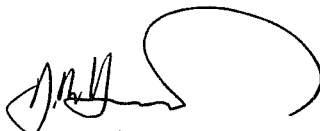
**Action to be taken**

You will find enclosed with this document a form of proxy for use at the Annual General Meeting at which a resolution to adopt the new plan will be proposed. Whether or not you propose to attend the meeting in person, you are requested to complete the form of proxy in accordance with the instructions printed on it and to return it as soon as possible to the Company's registered office so as to be received by no later than 48 hours before the time fixed for the meeting. Completion and return of a form of proxy will not prevent you from attending and voting at the meeting in person if you so wish.

**Recommendation**

Your Board considers that the resolution to adopt the new plan to be proposed at the Annual General Meeting is in the best interests of shareholders as a whole and recommends that shareholders vote in favour of the resolution.

Yours faithfully



**AM Howarth, Chairman**

## APPENDIX

### Summary of the principal features of the Gresham Computing plc 2007 Executive Option Plan (the Plan)

#### Introduction

Over the last year, the executive management team has taken many positive steps to position the Company to meet its objective of achieving long-term sustainable growth. Retaining and motivating the management team and other key employees is crucial to maintaining momentum. The Remuneration Committee (the **Committee**) has therefore undertaken a thorough review of the Company's share-based incentives to ensure they reinforce its business strategy, motivate the executive team to deliver superior shareholder returns and are competitive in our sector.

The Company currently operates an executive share option scheme (**ESOS**) and an all employee savings related share option scheme, both approved by shareholders in 1998. Under the ESOS, awards of share options are made to executive directors and other participants with vesting being subject to the achievement of a given level of growth in earnings per share over a three-year period.

The Committee considers that for long-term incentives to be most effective at Gresham, they must satisfy two key principles:

- provide clear line of sight between reward and performance outcomes; and
- provide strong alignment with the creation and delivery of value to shareholders.

Accordingly, the Board is seeking approval for the adoption of a new executive option plan which it believes satisfies these principles and which aims to reward executive directors and other key employees for achieving targeted returns over a three to five (or six) year period with a right to acquire new issue ordinary shares in the Company (**shares**).

No further awards would be made under the ESOS after adoption of the Plan, although unexercised options previously granted under the ESOS will remain exercisable in accordance with the scheme rules. A summary of outstanding ESOS options is provided in section 19.

The Committee believes that the proposed Plan is in the best interests of shareholders and will help the Company to attract, motivate and retain the talent it needs to drive its business forward. These proposals have the full support of the Committee and the Board as a whole.

Copies of the rules of the Plan will be available for inspection during normal business hours from Mondays to Fridays at the Company's registered office and at the offices of KBC Peel Hunt Ltd, 4th Floor, 111 Old Broad Street, London EC2N 1PH from the date of this letter until (and including) the date of the Annual General Meeting, and also at the place of the meeting for fifteen minutes prior to and during such meeting.

The principal features of the Plan are as follows:

#### 1. Constitution and administration

The Plan will be constituted by rules approved by the Committee and adopted by the directors. The Committee will determine from time to time whether and in what manner the Plan should be used.

#### 2. Participating companies

The Plan will extend to the Company and any of its subsidiaries and associated companies (each a **Group Company**).

#### 3. Eligibility

Any employee or director of the Company or any other Group Company for whom no UK income tax liability would arise on award grant will be eligible for participation in the Plan. However, it is the Committee's intention to restrict participation in the Plan to the Company's key executives, including the executive directors, to ensure awards are targeted at those employees best placed to drive achievement of the Company's strategic and financial goals.

#### 4. Award structure

Awards made under the Plan will be structured as stock appreciation rights (**SARs**) which give a participant the right to benefit from a rise in the market value of shares the subject of an award from date of grant to the relevant vesting date. On exercise, a participant will be required to pay the Company by way of subscription an amount equal to the aggregate nominal value of the shares to be issued to him. There will be no cash alternative available to participants but the Company anticipates that a cashless exercise facility may be made available to employees primarily to facilitate the payment by them of the exercise price and any tax due on exercise.

The Committee has considered a range of alternative approaches to funding long-term share incentives and has concluded that the approach proposed offers the best solution for shareholders and employees.

There will be two elements to each SAR award: a Basic award and, for every two Basic awards, a Bonus award, each exercisable on the achievement of the challenging performance targets described further in section 7 below.

The performance criteria are based on the achievement of fixed target Company share prices (**target share prices**), with a minimum target share price of £2.50 to be achieved before any Basic awards are exercisable and a price of £4.00 to be achieved before Bonus awards are exercisable. Unexercised awards will lapse six years from the date of grant.

It is intended that the majority of available awards will be granted on, or shortly after, adoption of the Plan by the Company. A smaller pool enabling the making of further awards will be held back for new joiners.

#### 5. Grant of awards

An award of SARs entitles the holder to acquire such number of shares as has a value equal to the increase in the market value of the shares subject to the award between the date of grant and the date of vesting. The strike price for each share comprised in an award at date of grant is to be determined by the Committee but will not be less than the average of the middle-market price of a share, as derived from The London Stock Exchange Daily Official List, on the three dealing days immediately preceding the appropriate date plus a premium of 10 pence for each such share.

An award of SARs may generally only be made within the period of 42 days commencing on:

- (a) the day on which the Plan is adopted by the Company; or
- (b) a day on which the Company makes an announcement of its results for any year, half year or other period.

An award may also be made within 14 days of a Group Company recruiting a new employee.

#### 6. Individual limits

An eligible participant will, other than in the case of any adjustments made to reflect a promotion or significant change in responsibilities, receive only one grant of awards under the Plan. The maximum aggregate market value of the Basic component of an award at date of grant to any participant will not exceed an amount being equal to six times basic salary.

It is proposed that 50% of the total number of awards will be allocated to directors of the Company and the remaining 50% to senior management.

#### 7. Performance conditions and re-testing

##### **Basic awards**

Basic awards will vest, subject to the achievement of target share prices, in one-third increments over each of the third, fourth and fifth years from date of grant respectively (each a **Basic Performance Period**) as follows:

- one-third at the end of year 3 for achieving a target share price of £2.50;
- one-third at the end of year 4 for achieving a target share price of £3.00; and
- one-third at the end of year 5 for achieving a target share price of £4.00.

### **Bonus awards**

Bonus awards will be granted as to one Bonus award for every two Basic awards and will vest in full, subject to achievement of a target share price of £4.00, at the end of the fifth year from date of grant (the **Bonus Performance Period**).

### **General**

When assessing the achievement of target share prices, the Company's share price performance will be calculated based on the average middle-market price of a share, as derived from The London Stock Exchange Daily Official List, on the twenty dealing days immediately preceding each of the third, fourth and fifth anniversaries of the date of grant, as appropriate.

Any SARs the subject of a Basic or Bonus award which do not become exercisable in full according to performance measured over the relevant Basic or Bonus Performance Period will nevertheless become exercisable to the extent that one or more of the target share prices described above are achieved on average in any consecutive 20 dealing day period from the fifth to the sixth anniversaries of grant. Any SARs subject to a Basic or Bonus award which remain unexercisable after this second test of the performance conditions will lapse.

The Committee believes that linking vesting of SAR awards to target share prices helps ensure the incentive is (i) a robust measure of management performance; (ii) motivational for participants; and (iii) strongly aligned with shareholder interests.

The Committee recognises that it is not strictly in accordance with generally accepted institutional guidelines for a listed UK company to grant long-term incentives which allow for a "re-test" of performance. However, it is intended that ordinarily the Plan be "one-off" rather than "rolling" (ie. allowing for annual grants) as would typically be the nature of such plans. Additionally, the share price performance condition takes no account of the impact of a general decline in the wider market or one off events affecting price that are outside the Company's control. Consequently, the Committee considers the re-test to be an essential feature of the Plan to help ensure it is robust to short-term fluctuations in performance and market conditions around the measurement dates and hence, is able to remain motivational to participants.

In limited circumstances, the Committee proposes to reserve the discretion to adjust the performance conditions set under the Plan. This discretion would not be exercised so as to make changes that are to the material advantage of participants without obtaining the prior approval of shareholders in general meeting. Any amendment of performance conditions not previously approved by shareholders will be described in the report and accounts for the relevant year.

## **8. Exercise of awards**

As described above, Basic awards would normally become capable of exercise in one-third increments after three, four and five years from date of grant respectively. Bonus awards would normally become capable of exercise five years after the date of grant. Exercise of Basic and Bonus awards is in any event subject to achievement of the challenging performance targets described in section 7. The exercise price payable is the nominal value of each share to be issued to a participant.

An award may only be exercised by the participant to whom it was granted, or (on death and only in respect of any vested but unexercised awards) his personal representative(s) during the preceding period of twelve months, and will not be transferable.

If a participant in the Plan ceases to be employed by a Group Company before any part of his award becomes vested for any reason other than voluntary resignation or dismissal for gross misconduct (but not otherwise), the Committee will have discretion to allow all or part vesting of that part of his Basic award, and Bonus award depending on the timing, which is next in time to vest according to such formula as it sees fit which will measure the performance of the Company over the period from date of grant until cessation of employment.

In the event of a takeover or proposal for a scheme of arrangement of the Company (not being an internal corporate reorganisation), the Committee will accelerate vesting of a participant's Basic and Bonus awards according to a formula which assesses the target share price performance condition as at the date the relevant transaction becomes or is declared wholly unconditional or otherwise completes as if all of the Basic and Bonus Performance Periods had elapsed at that date.

Alternatively, following a takeover awards may, with the agreement of the acquiring company and the consent of the participant, be rolled-over to become awards over the acquiring company's shares. In the absence of roll-over or exercise as above, awards will lapse.

## 9. Lapse of awards

Awards will lapse on cessation of employment other than in the circumstances referred to above or if awards are not exercised within the prescribed periods. Awards will also lapse to the extent that the relevant target share prices are not satisfied at the end of the relevant performance periods or on any re-test.

## 10. Dilution

Awards made under the Plan will be satisfied through the issue by the Company of new shares. If the entire allocation of Basic and Bonus awards were granted, a maximum of 10% of the current issued ordinary share capital of the Company would be required to satisfy awards made, although dilution to the 10% level would require share price performance significantly ahead of the performance conditions described in section 7. Achievement of the target share prices set out in the table below would give rise to a dilution of approximately 6.1% where all performance criteria are met but not exceeded, or less than 3% dilution where the highest target share price is not achieved (and as a consequence no Bonus awards vest).

It is not possible to determine the precise level of dilution until a SAR is exercised at which point actual dilution will depend on the Company's then prevailing share price.

Dilution from options granted over the last eight years under the Company's existing employee share schemes is approximately 5% of current total issued ordinary share capital. Consequently, during the next five to six years, dilution from awards granted under all the Company's share schemes will not exceed 15% of its current issued share capital, and will not exceed 10% other than for exceptional performance. The number of SAR awards made and the actual levels of dilution which occur will be disclosed each year in the Company's annual report and accounts.

The following table shows (purely for illustrative purposes) both the total level of dilution which would apply under different average increases in share price and, for comparative purposes, the potential level of return to shareholders achieved under various performance scenarios:

Actual prices achieved £			Shares issued	Dilution	Mkt value increase £m
Year 3	Year 4	Year 5			
1.50	1.50	1.75	0	0.0%	40
2.50	2.60	2.75	537,600	1.1%	86
2.50	3.00	3.25	1,172,267	2.3%	116
2.50	3.00	4.00	3,062,267	6.1%	166

The bases and sources of the information set out above are as follows:

- total issued share capital: 50,350,890 shares;
- SAR awards granted: basic 3,360,000 and bonus 1,680,000;
- target share prices:
  - Year 3 £2.50
  - Year 4 £3.00
  - Year 5 £4.00
- strike price per share: £1.30 (10 pence premium to an assumed £1.20 market price); and
- the dilution calculation assumes that all awards are granted immediately following adoption of the Plan and that the maximum exercise takes place as soon as each target share price is achieved.

The Committee recognises that the level of dilution resulting from awards made under the Plan may exceed the generally accepted institutional guideline that no more than 10% of a company's issued ordinary share capital may be awarded under employee share schemes in any ten year rolling period. However, the Committee believes that the overall structure of the Plan, its performance

conditions and its potential value to participants will create a powerful incentive for the executive team to achieve the Company's business goals and create value for shareholders. The Committee notes that dilution will remain below 10% except where the increase in shareholder return is exceptional, requiring over-achievement of the stretching target share prices outlined in section 7.

#### **11. Pension implications**

The value of any awards granted or shares issued under the Plan will not be pensionable.

#### **12. Tax implications**

The Plan will not be approved by HM Revenue & Customs. For employees subject to UK taxation, income tax and national insurance contributions (**NICs**) will both be payable on the difference between the share price at date of grant and the market price at the date of exercise. A condition of exercise is that each employee shall meet any employment tax liabilities arising from the Plan, including but not restricted to employer's NICs, income tax and similar taxes.

#### **13. Amendments**

The Plan may be amended by the Committee in any way with the previous sanction of the Company in general meeting provided that minor amendments may be made by the Committee to benefit the administration of the Plan, to comply with or take account of a change in legislation or to obtain or maintain favourable tax, exchange control or regulatory treatment for eligible participants or any Group Company.

#### **14. Overseas employees**

The directors may (to the extent deemed necessary) establish further plans for non-UK employees based on the Plan but modified (if required) to take account of local taxation, securities laws and other regulatory requirements. SARs allocated under these plans will count against the overall and individual limits set out in the Plan.

#### **15. Termination**

The Plan will terminate on the tenth anniversary of the date of its approval by shareholders or at any earlier time by resolution of the directors, but the rights of existing participants will not thereby be affected.

#### **16. Issue of shares**

Shares issued under the Plan will rank *pari passu* with the shares then in issue other than in respect of dividend and other entitlements arising by reference to a record date falling prior to the date of exercise. As soon as practicable after the allotment of any shares, application will be made to the UK Listing Authority for their admission to the Official List.

#### **17. Issues and reorganisations of capital**

The rights of participants following any rights issue, capitalisation issue or other reconstruction or variation of capital will be adjusted as relevant and where appropriate in such manner as the Committee may reasonably determine.

#### **18. Rights in respect of SARs**

Participants will not have any shareholder rights in respect of unexercised SARs the subject of an award.

## 19. Existing rights in respect of ESOS

Outstanding options to subscribe for shares under the ESOS as at 31 December 2006 were as follows:

<b>Number of share options</b>	<b>Date of grant</b>	<b>Exercise price £</b>	<b>Date first exercisable</b>	<b>Expiry date</b>
43,919	17-Feb-99	1.420	18-Feb-02	17-Feb-09
10,000	09-Feb-00	0.460	10-Feb-03	09-Feb-10
637,897	25-Jul-00	0.360	28-Jul-03	27-Jul-10
12,500	22-Apr-03	0.700	23-Apr-06	22-Apr-13
20,000	28-May-04	3.225	29-May-07	28-May-14
49,998	22-Jun -05	1.200	23-Jun-08	22-Jun-15
10,000	30-Sep-05	0.860	01-Oct-08	30-Sep-15
<b><u>784,314</u></b>				

The above analysis includes 557,897 options held by AJS Walton-Green which were granted on 25 July 2000 with an exercise price of £0.360 and are exercisable between 28 July 2003 and 27 July 2010.