

Spark New Zealand Limited

Appraisal Report

In Respect of the Managing Director's Equity-based Incentive Schemes

September 2015

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1. Introduction

1.1 Background

Spark New Zealand Limited (**Spark NZ** or the **Company**) is listed on the main equities securities market (the **NZX Main Board**) operated by NZX Limited (**NZX**) with a market capitalisation of \$5.5 billion as at 30 September 2015 and audited total equity of \$1.8 billion as at 30 June 2015.

The Company was formed in 1987 out of the telecommunications division of the New Zealand Post Office, a government department.

On 30 November 2011, the Company demerged into 2 separate companies listed on the NZX Main Board:

- Spark NZ – a retail services provider
- Chorus Limited – a network services operator.

Spark NZ is one of New Zealand’s largest listed companies, providing communications services and products to New Zealanders, New Zealand businesses and others.

1.2 Managing Director Remuneration

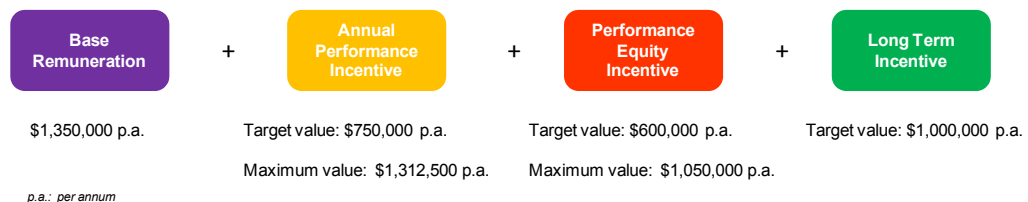
Appointment of Managing Director

Spark NZ announced on 23 April 2012 that it had appointed Simon Moutter to the role of Managing Director of Spark NZ. Mr Moutter commenced in the role on 13 August 2012.

Remuneration Package

Mr Moutter and Spark NZ entered into an employment agreement dated 22 April 2012 (the **Employment Agreement**).

Mr Moutter’s remuneration consists of a mixture of fixed remuneration plus short term and long term incentive remuneration. The key components of his remuneration package are set out below. The remuneration package is reviewed annually and has remained at the same level since Mr Moutter’s appointment.



Annual Performance Incentive

Mr Moutter's remuneration package includes an annual short term performance incentive in the form of \$750,000 in cash if he meets the targets (the **Targets**) set by Spark NZ's board of directors (the **Board**).

The annual short term performance incentive cash payment may increase if Mr Moutter significantly exceeds the Targets, up to a maximum of \$1,312,500 per annum (being 175% of the target value).

Performance Equity Incentive

Mr Moutter's remuneration package also includes an annual performance equity incentive in the form of redeemable ordinary shares with a target value of \$600,000 for achievement of the Targets (the **MD Performance Equity Scheme**).

The value of the award under the MD Performance Equity Scheme may increase if Mr Moutter significantly exceeds the Targets, up to a maximum of \$1,050,000 of redeemable ordinary shares per annum (being 175% of the target value).

Long Term Incentive

Mr Moutter is also eligible for a long term incentive of \$1,000,000 annually in the form of restricted shares (the **MD Long Term Incentive Scheme**).

A subsidiary of Spark NZ will loan Mr Moutter an amount equal to the net (after tax) issue value, interest-free, which will be advanced to Spark Trustee Limited (the **Trustee**) and used by the Trustee to purchase restricted shares in Spark NZ. The shares will be held by the Trustee for a set restrictive period of 3 years.

At the end of the restrictive period:

- if the performance hurdle is met and all of the restricted shares are eligible to vest, or no performance hurdle applies, a cash bonus will be paid to Mr Moutter (being the grossed up value of the original issue value), the net proceeds of which will be applied to repay the loan and any residual amount will be paid to Mr Moutter
- if the performance hurdle is not met, then the Trustee will purchase the restricted shares from Mr Moutter at the original issue value and the proceeds of which will be applied to repay the loan.

The proposed MD Long Term Incentive Scheme differs to some degree from the previous MD Long Term Incentive Scheme that was implemented in 2012 insofar as the previous MD Long Term Incentive Scheme granted performance rights to Mr Moutter as opposed to issuing restricted shares.

We refer to the MD Performance Equity Scheme and the MD Long Term Incentive Scheme collectively as the **MD Share Schemes**.

Annual Review of Remuneration

Mr Moutter's total remuneration is reviewed at the end of each financial year. The target values and amounts set out above apply for the 2016 financial year and subsequent payments and issues of shares may be based on revised target values in line with any future adjustment to Mr Moutter's remuneration package and components.

1.3 Regulatory Requirements

Listing Rule 7.3.1 of the NZX Main Board Listing Rules states that no Issuer shall issue any Equity Securities unless the precise terms and conditions of the specific proposal to issue those Equity Securities have been approved by separate resolutions (passed by a simple majority of votes) of holders of each Class of Quoted Equity Securities of the Issuer whose rights or entitlements could be affected by that issue.

NZX Main Board Listing Rule 6.2.2(b) requires an Appraisal Report to be prepared where a meeting will consider a resolution where more than 50% of the securities to be issued will be acquired by directors of the Issuer.

NZX Main Board Listing Rule 7.6.5 states that an Issuer may provide financial assistance in connection with the acquisition of Equity Securities if the precise terms and conditions of a specific proposal to provide financial assistance have been approved by a resolution of members of each separate group of each Class of Quoted Equity Securities of the Issuer whose rights or entitlements are materially affected in a similar way by the proposal (in this case, the holders of Spark NZ's ordinary shares).

NZX Main Board Listing Rule 6.2.2(c) requires an Appraisal Report to be prepared where more than 50% of the total financial assistance to be given is provided to directors or associated persons of directors of the Issuer.

Listing Rule 10.14 of the ASX Limited (**ASX**) Listing Rules states that an entity must not permit a director of the entity to acquire securities under an employee incentive scheme without the approval of holders of ordinary securities of the acquisition.

ASX Listing Rule 10.14 requires that the notice of meeting to obtain approval must comply with ASX Listing Rule 10.15A which mandates a number of disclosures such as the maximum number of securities that may be acquired and the formula for calculating the number of securities to be issued.

1.4 Annual Meeting of Shareholders

Shareholders will vote on 2 ordinary resolutions in respect of the MD Share Schemes at Spark NZ's annual meeting of shareholders on 6 November 2015:

- the issue to Mr Moutter during the 3 year period to 5 November 2018 of in total up to 1,000,000 shares in Spark NZ under the MD Performance Equity Scheme (comprising redeemable ordinary shares and, where contemplated by the scheme, ordinary shares) (resolution 4)
- the issue to Mr Moutter during the 3 year period to 5 November 2018 of in total up to 1,250,000 restricted shares in Spark NZ under the MD Long Term Incentive Scheme and an associated interest-free loan of up to \$3,000,000 (resolution 5).

Only the Company's shareholders not associated with Mr Moutter (the **Non-associated Shareholders**) may vote on the resolutions.

1.5 Purpose of the Report

The directors of Spark NZ not associated with Mr Moutter (the **Non-associated Directors**) have engaged Simmons Corporate Finance Limited (**Simmons Corporate Finance**) to prepare an Appraisal Report on the fairness of the MD Share Schemes in accordance with NZX Main Board Listing Rules 6.2.2(b) and 6.2.2(c).

Simmons Corporate Finance was approved by NZX Regulation on 14 August 2015 to prepare the Appraisal Report.

Simmons Corporate Finance issues this Appraisal Report to the Non-associated Directors for the benefit of the Non-associated Shareholders to assist them in forming their own opinion on whether to vote for or against the resolutions in respect of the MD Share Schemes.

We note that each shareholder's circumstances and objectives are unique. Accordingly, it is not possible to report on the fairness of the MD Share Schemes in relation to each shareholder. This report on the fairness of the MD Share Schemes is therefore necessarily general in nature.

The Appraisal Report is not to be used for any other purpose without our prior written consent.

All references to \$ are to New Zealand dollars.

2. Evaluation of the Fairness of the MD Share Schemes

2.1 Basis of Evaluation

NZX Main Board Listing Rule 1.7.2 requires an Appraisal Report to consider whether the consideration and the terms and conditions of the MD Share Schemes are *fair* to the Non-associated Shareholders.

There is no legal definition of the term *fair* in New Zealand in either the NZX Main Board Listing Rules or in any statute dealing with securities or commercial law.

In our opinion, the MD Share Schemes will be fair to the Non-associated Shareholders if:

- the shares issued to Mr Moutter under the MD Share Schemes represent a fair level of incentive remuneration to Mr Moutter when viewed as part of his total remuneration package
- the terms and conditions of the MD Share Schemes are fair
- there are no material negative impacts on the Non-associated Shareholders.

We have evaluated the fairness of the MD Share Schemes by reference to:

- the rationale for the MD Share Schemes
- the value of the MD Share Schemes to Mr Moutter
- the terms and conditions of the MD Share Schemes
- the impact of the MD Share Schemes on shareholding levels
- the impact of the MD Share Schemes on Spark NZ's share price.

Our opinion should be considered as a whole. Selecting portions of the evaluation without considering all the factors and analyses together could create a misleading view of the process underlying the opinion.

2.2 Opinion on the Fairness of the MD Share Schemes

In our opinion, after having regard to all relevant factors, the consideration and the terms and conditions of the MD Share Schemes are fair to the Non-associated Shareholders.

The basis for our opinion is set out in detail in sections 2.3 to 2.10. In summary, the key factors leading to our opinion are:

- the rationale for the MD Share Schemes is sound. The MD Performance Equity Scheme and the MD Long Term Incentive Scheme seek to provide long term equity incentives to Mr Moutter which align his interests with those of the Non-associated Shareholders
- the overall remuneration level for Mr Moutter appears to be reasonable and has not changed since Mr Moutter was first appointed to the role of Managing Director in 2012

- the terms and conditions of the MD Performance Equity Scheme are reasonable:
 - the issue of equity in the form of redeemable ordinary shares aligns Mr Moutter's interests with those of the Non-associated Shareholders
 - the Targets (assuming they are similar to those adopted in recent times) represent a reasonable basis upon which to evaluate Mr Moutter's performance and to determine the level of incentive award
 - the redeemable ordinary shares are subject to a 2 year restrictive period where Mr Moutter cannot dispose of the shares
 - the redeemable ordinary shares can be redeemed by Spark NZ in certain circumstances if Mr Moutter ceases to be employed by the Company
 - the MD Performance Equity Scheme will only have value to Mr Moutter to the degree that the Targets are met. To the extent that the Targets are not met, then Mr Moutter will derive reduced value from the scheme
- the terms and conditions of the MD Long Term Incentive Scheme are reasonable:
 - the issue of equity in the form of restricted shares aligns Mr Moutter's interests with those of the Non-associated Shareholders
 - the Performance Hurdle (based on absolute total shareholder return (TSR) for the issue in the 2016 financial year) is an appropriate basis upon which to determine whether the restricted shares vest
 - the vesting period of 3 years after each issue date provides a suitably long term incentive period
 - the MD Long Term Incentive Scheme will only have value to Mr Moutter if the Performance Hurdle is met. In the event that the Performance Hurdle is not met, then no restricted shares will vest and Mr Moutter will derive no value from the scheme
- the potential dilutionary impact of the MD Share Schemes on Non-associated Shareholders is negligible at 0.12%
- the shares issued under the MD Share Schemes are unlikely to have any material impact on Spark NZ's share price or the liquidity of its shares
- if the resolutions in respect of the MD Share Schemes are not approved, then each entitlement will be paid in cash at the equivalent value. The cash payments will be subject to the same terms and conditions to which any equity would have been subject and will be paid at the same time as any entitlements in respect of equity would have vested.

2.3 Rationale for the MD Share Schemes

In general terms, companies provide equity-based long term executive incentive remuneration to tie executives' remuneration to the annual and long term performance of the company and to align the interests of the executives with those of shareholders. Key perceived benefits to the company include:

- equity-based long term executive incentive remuneration helps to attract and retain top executives
- it enables executives to build equity ownership in the company
- executives' interests are more closely aligned with shareholders' interests.

There has been growing criticism in New Zealand and abroad in respect of the equity-based incentive remuneration. The criticisms centre around:

- the lack of performance hurdles and / or inadequate explanation of performance hurdles
- the length of term for the equity-based incentive remuneration being too short and hence not aligning with shareholder interests
- already generous remuneration for executives.

In structuring Mr Moutter's remuneration package, the Board aimed to create an appropriate balance between the fixed and variable components so that a substantial proportion of Mr Moutter's remuneration related to his performance and that of the Company. The Board also ensured that a significant proportion of Mr Moutter's remuneration package would be paid through the issue of equity securities to align his interests with those of the Non-associated Shareholders.

In our view, the rationale for the MD Share Schemes as a component of Mr Moutter's remuneration package is sound:

- it is designed to align the interests of Mr Moutter with those of the Non-associated Shareholders, with just under half of his annual remuneration package being payable in the form of equity
- it forms an integral component of Mr Moutter's variable remuneration, which represents almost two thirds of his total remuneration package
- it aims to provide a long term incentive, thus aiding in the retention of Mr Moutter.

2.4 Mr Moutter's Remuneration Package

Although the focus of our evaluation is primarily on the MD Share Schemes, consideration needs to be given to the overall level of remuneration for Mr Moutter.

A summary of Mr Moutter's target remuneration for the 2016 financial year is set out below.

Mr Moutter's Target Remuneration for the 2016 Financial Year				
	Cash (\$000)	Equity (\$000)	Total	
			(\$000)	%
Fixed remuneration	1,350	-	1,350	36.5%
Variable remuneration				
Annual performance incentive	750 ¹	-	750	20.3%
MD Performance Equity Scheme	-	600 ¹	600	16.2%
MD Long Term Incentive Scheme	-	1,000	1,000	27.0%
Total	750	1,600	2,350	63.5%
Total remuneration	2,100	1,600	3,700	100.0%
- %	56.8%	43.2%		

¹ Based on 100% of target value

The annual performance incentive and MD Performance Equity Scheme amounts are based on the Targets being met (but not exceeded).

The level of annual variable remuneration from the annual performance incentive and the MD Performance Equity Scheme can vary from nil (based on the Targets not being met at all) to 175% of the target values:

- annual performance incentive – nil to \$1,312,500
- MD Performance Equity Scheme – nil to \$1,050,000.

Key features of the remuneration package are:

- approximately one third of the total target remuneration package is fixed remuneration and the remainder is variable
- just under half of the total target remuneration package is payable in equity with the remainder payable in cash.

In initially setting the remuneration package in 2012, the Board obtained advice from PricewaterhouseCoopers (**PwC**) on remuneration levels for CEOs of similar sized organisations. In its report entitled *CEO Market Remuneration Assessment Report* dated 1 May 2012 (the **PwC Remuneration Report**), PwC opined that the proposed remuneration package for Mr Moutter was reasonable. PwC considered the level of base remuneration to be reasonable and the mix of fixed and variable remuneration to be largely consistent with comparator companies. A summary of the advice provided by PwC to the Board was included in Spark NZ's 2012 notice of annual meeting.

Mr Moutter's remuneration is disclosed each year in Spark NZ's annual report. The level of disclosure is relatively comprehensive, with a breakdown of the remuneration component amounts and references to the Company's website where detailed explanations of the terms of the remuneration components can be found.

The structure of Mr Moutter’s performance-related variable remuneration components means that his remuneration is likely to vary significantly from year to year. Mr Moutter’s remuneration levels for the 2013, 2014 and 2015 financial years are set out below.

Mr Moutter’s Remuneration Levels for the Past 3 Years			
Financial Year	2013¹	2014	2015
Base salary ²	1,194,231	1,358,736	1,411,036
Annual performance incentive	271,274	1,132,500	825,000
MD Performance Equity Scheme	217,019	906,000	660,000
MD Long Term Incentive Scheme	1,750,000 ³	1,981,494 ⁴	1,000,000
Total	<u>3,432,524</u>	<u>5,378,730</u>	<u>3,896,036</u>

¹ Pro rated from the date of Mr Moutter’s commencement of employment
² Includes employer contributions towards KiwiSaver
³ Includes \$750,000 in the form of 299,390 performance rights which were awarded as a one-off grant at the commencement of Mr Moutter’s employment
⁴ Includes \$981,494 in the form of 428,600 performance rights granted on 15 November 2013 as a one-off exceptional grant with substantially more challenging performance hurdles attached
 Source: Spark NZ annual reports

Mr Moutter’s remuneration package (including annual target values of the incentive components of his package) is reviewed annually at 1 July by the Board. The remuneration package has remained at its initial level each year and will be at this level for the 2016 financial year.

2.5 Terms of the MD Performance Equity Scheme

Overview

The terms of the MD Performance Equity Scheme are set out in the explanatory notes on pages 4 and 5 of the notice of annual meeting. They are not included in detail in this report so as to avoid repetition.

The objective of the MD Performance Equity Scheme is to reward Mr Moutter for achieving pre-specified target levels of performance during a financial year (ie the Targets). This component of his remuneration is structured in the form of the issue of redeemable ordinary shares so as to link it to the long term performance of the Company.

The maximum number of shares to be issued to Mr Moutter over the 3 year period to 5 November 2018 for which shareholder approval is sought is 1,000,000 shares. This includes all redeemable ordinary shares and any ordinary shares to be issued.

Assuming the MD Performance Equity Scheme is approved by the Non-associated Shareholders, the first issue of redeemable ordinary shares under the MD Performance Equity Scheme will occur in September 2016, following determination by the Board of the actual incentive award achieved in respect of the 2016 financial year and the announcement of Spark NZ’s results for the 2016 financial year.

Subsequent issues of shares will be at the discretion of the Board (within the context of the approval granted by Non-associated Shareholders) and may be made in September of each year but in no case will shares be issued later than 3 years after the date of the 2015 annual meeting (unless a further shareholder approval is obtained).

Our evaluation of the key terms of the MD Performance Equity Scheme is set out below.

Redeemable Ordinary Shares

The redeemable ordinary shares have the same rights and terms as the ordinary shares except that during the restrictive period (discussed below) they can be redeemed (ie acquired from Mr Moutter and cancelled by Spark NZ) for a nominal consideration of \$1 in certain circumstances.

The redeemable ordinary shares will automatically reclassify into ordinary shares at the end of the specified period to which the trading restrictions apply.

Targets and Determination of Incentive Award

The amount of any incentive award under the MD Performance Equity Scheme will depend on the Board's evaluation of Mr Moutter's performance measured against the Targets. The Board will prescribe the Targets for each financial year in consultation with Mr Moutter.

If Mr Moutter achieves the Targets in any financial year, he will be entitled to an incentive award equal to the annual target value of the MD Performance Equity Scheme. The annual target value for the 2016 financial year is \$600,000. The amount of the incentive award will be adjusted up or down in line with assessed over or under performance. The maximum pre tax value of the incentive award is capped at 175% of the annual target value.

Historically, the Targets have included overall financial targets (such as earnings before interest, tax, depreciation and amortisation (**EBITDA**)), specific performance objectives based on Spark NZ's business and strategic plans and other criteria relating to corporate governance, reputation, effective leadership and management. We are advised that the Targets for the 2016 financial year are based on EBITDA and targeted cash savings levels.

We are of the view that the Targets represent appropriate bases upon which to evaluate Mr Moutter's performance and determine the level of incentive award to be paid to him under the MD Performance Equity Scheme.

Number of Shares Issued

The number of redeemable ordinary shares issued will be calculated by dividing the after tax value of the incentive award by the volume weighted average market price (**VWAP**) of Spark NZ's ordinary shares reported on the NZX Main Board for the 20 trading days immediately preceding the effective date of issue of the redeemable ordinary shares.

The shares are subject to the trading restrictions discussed in the following section.

Trading Restrictions

Mr Moutter cannot transfer, assign or otherwise dispose of the redeemable ordinary shares for a specified period following their issue.

The redeemable ordinary shares issued in respect of the 2016 financial year cannot be sold or otherwise disposed of for a 2 year period following their issue in September 2016.

The Board may specify longer or shorter restrictive periods for subsequent issues.

In our view, the restrictive period of 2 years (following the initial performance period of one year which determines the amount of the award) is a suitable mechanism to aid in the retention of Mr Moutter and to align his interests with those of the Non-associated Shareholders.

Redemption of Shares

During the period in which the restrictions on disposal apply, the redeemable ordinary shares can be redeemed for an aggregate consideration of \$1 in certain circumstances where Mr Moutter's employment ceases. These circumstances are explained in the explanatory notes on page 5 of the notice of annual meeting.

This redemption feature ensures that Spark NZ can recover the shares if Mr Moutter ceases to be entitled to some or all of the shares during the relevant period.

Remuneration May be Paid in Cash

The Board may, in its sole discretion, determine that 100% of the incentive award will be received by Mr Moutter in cash instead of shares. Furthermore, if shareholder approval of the MD Performance Equity Scheme is not obtained, 100% of the incentive award will be received by Mr Moutter in cash instead of shares.

2.6 Terms of the MD Long Term Incentive Scheme

Overview

The terms of the MD Long Term Incentive Scheme are set out in the explanatory notes on pages 5 to 7 of the notice of annual meeting. They are not included in detail in this report so as to avoid repetition.

The objective of the MD Long Term Incentive Scheme is to link a portion of Mr Moutter's remuneration with the long term performance of Spark NZ and thereby align his interests with those of the Non-associated Shareholders through the issue of restricted shares.

The ability of any of the restricted shares to vest and the number of restricted shares that will vest following the end of the restrictive period is dependent on achievement of the Performance Hurdle.

The maximum number of restricted shares to be issued to Mr Moutter over the next 3 year period to 5 November 2018 for which shareholder approval is sought is 1,250,000 restricted shares.

Assuming the MD Long Term Incentive Scheme is approved by the Non-associated Shareholders, the first issue of restricted shares is expected to occur in November 2015.

Subsequent issues of restricted shares will be at the discretion of the Board (within the context of the approval granted by the Non-associated Shareholders) and may be made in September of each year but in no case later than 3 years after the date of the 2015 annual meeting (unless a further shareholder approval is obtained).

Our evaluation of the key terms of the MD Long Term Incentive Scheme is set out below.

Restricted Shares

The restricted shares will be issued to the Trustee and held for Mr Moutter for the restrictive period. The restricted shares cannot be sold, transferred or otherwise disposed of by Mr Moutter during this restrictive period.

The restricted shares will have the same dividend rights as all other ordinary shares. However, any dividends received during the restrictive period are required to be applied to repay the loan provided by Spark NZ to Mr Moutter to acquire the restricted shares.

Financial Assistance

Mr Moutter will be loaned an interest-free amount equal to the after tax value of the target value which will be advanced to the Trustee and applied to the purchase or issue of the restricted shares. Spark NZ's recourse in respect of the loan will be limited to the shares acquired with the loan.

The interest-free loan amounts to \$670,000 per annum, being the before tax target value of \$1,000,000 less tax at the top marginal rate of 33%.

Upon the vesting of the restricted shares, Mr Moutter will be paid a cash bonus equal to the grossed-up value of the original loan, which after the deduction of tax, will be applied to repay the outstanding balance of the loan and the shares will transfer from the Trustee to Mr Moutter.

Number of Shares Issued

The number of restricted shares issued will be calculated by dividing the after tax target value of the issue (\$670,000) by the VWAP of Spark NZ's ordinary shares reported on the NZX Main Board for the 20 trading days immediately preceding the effective date of the issue of the restricted shares.

Restrictive Period

The Board sets the period after which restricted shares are eligible for vesting (ie the shares become unrestricted and transfer to Mr Moutter).

For the 2016 financial year, the Board has determined that the restricted shares will be eligible for vesting in September 2018. For subsequent share issues, it is anticipated that the Board will specify that the restricted shares will be eligible for vesting on the third anniversary of their issue.

In our view, the vesting of the restricted shares 3 years after their respective issue dates is an appropriate period to ensure that the MD Long Term Incentive Scheme provides a suitable long term incentive to Mr Moutter.

Performance Hurdle

The Board will determine each year the Performance Hurdle that will apply to restricted shares issued under the MD Long Term Incentive Scheme.

Restricted shares will only vest and be transferred to Mr Moutter if the applicable Performance Hurdle has been met.

2016 Performance Hurdle Based on Absolute TSR

For the restricted shares that will be issued in the 2016 financial year, the relevant shares will only transfer to Mr Moutter if Spark NZ's absolute TSR for the restrictive period meets or exceeds Spark NZ's cost of equity plus a margin of 1.0%, compounded annually (the **LTI 2016 Target**).

TSR is a measure of the combination of share price appreciation and dividends paid over a defined period. TSR calculations for the LTI 2016 Target will be made with reference to the closing price immediately prior to the effective date of the issue of the restricted shares and the VWAP of the Company's shares for the 10 business days at the end of the restrictive period.

If Spark NZ's TSR performance meets or exceeds the LTI 2016 Target, all of the restricted shares will transfer to Mr Moutter.

If Spark NZ's TSR performance does not meet the LTI 2016 Target, then all of the restricted shares will lapse.

Reasonableness of Performance Hurdle

The Board's objective is to align Mr Moutter's long term incentive remuneration with Spark NZ's performance. There are a variety of measures to assess a company's financial performance. TSR is one such measure. Others include return on equity, return on capital employed and growth in earnings per share (**EPS**).

TSR focuses on returns whereas EPS reflects growth more than returns (because it does not fully take into account the cost of capital employed to generate those earnings).

We have reviewed a range of executive remuneration packages for listed companies in New Zealand and Australia, as well as research on long term incentive plans in overseas companies. The majority of companies use either TSR or EPS (or a combination thereof) to set performance hurdles or set exercise prices for options. In doing so, companies use either relative performance hurdles (eg TSR benchmarked against the TSR of a basket of comparable companies or growth in EPS benchmarked against price indices such as the Consumer Price Index or Retail Price Index) or absolute performance hurdles (eg TSR and / or EPS growth based on predefined growth levels). In some circumstances where companies use more than one performance hurdle, they combine a relative performance hurdle (eg TSR) with an absolute performance hurdle (eg EPS growth).

In our view, the use of absolute TSR is an appropriate performance hurdle for the MD Long Term Incentive Scheme. While more sophisticated performance measures could be implemented (eg a combination of absolute and relative TSR or a combination of TSR and EPS growth benchmarked on a relative basis), we believe the benefits of the simplicity and transparency of using absolute TSR more than outweigh any benefits that may be gained from a more complex multi-measure approach.

The LTI 2016 Target requires Spark NZ's TSR to meet or exceed the Company's cost of equity plus a margin of 1.0%, compounded annually. Therefore in order for the restricted shares to vest, Spark NZ will need to generate actual returns for shareholders (TSR) over the restrictive period that are at least 1.0% (compounded annually) higher than the Company's shareholders' required rate of return (Spark NZ's cost of equity).

Spark NZ's cost of equity has recently been assessed by 9 equity research firms to range from 9.00% to 12.35%. The average of the assessments is 10.36%.

The Board will determine the Performance Hurdle to apply each year. We note that under the terms of the MD Long Term Incentive Scheme, the Board has discretion to issue restricted shares with no performance hurdles.

Restricted Shares Lapse Upon Termination of Employment

Mr Moutter's non-vested restricted shares lapse immediately upon termination of his employment, except in certain circumstances as explained in the explanatory notes on pages 6 and 7 of the notice of annual meeting.

Cash Payment Alternative

The Board may, in its sole discretion, determine that a cash amount equal to the value of the shares can be paid instead of issuing the restricted shares.

2.7 Impact on Shareholding Levels

Share Capital and Shareholders

Spark NZ has 1,830,581,956 fully paid ordinary shares on issue as at the date of this report (held by 28,211 shareholders as at 25 September 2015).

Mr Moutter currently holds interests in 2,077,244 shares in Spark NZ (including share rights), representing 0.11% of the Company's ordinary shares and share rights on issue at the date of this report:

- 511,608 ordinary shares
- 318,601 redeemable ordinary shares
- 1,247,035 share rights.

Maximum Number of Shares

Shareholder approval is being sought for the issue of a maximum of 2,250,000 shares under the MD Share Schemes in the 3 years to 5 November 2018:

- in total up to 1,000,000 shares under the MD Performance Equity Scheme
- in total up to 1,250,000 shares under the MD Long Term Incentive Scheme.

Shareholding Control

Assuming the maximum of 2,250,000 shares are issued to Mr Moutter under the MD Share Schemes, the redeemable ordinary shares are reclassified into ordinary shares, all share rights currently on issue are able to be exercised and no other shares are issued by the Company, there will be 1,836,962,933 ordinary shares on issue. Mr Moutter will hold 4,327,244 ordinary shares, representing 0.24% of the ordinary shares on issue.

In our view, Mr Moutter's maximum potential shareholding of 0.24% will have no material impact on his ability to exercise shareholder voting control.

Dilutionary Impact

Assuming the maximum of 2,250,000 shares are issued under the MD Share Schemes, this will result in the Non-associated Shareholders' proportionate shareholdings in the Company being diluted by 0.12%.

We do not consider this level of dilution to be of any significance to Non-associated Shareholders.

2.8 Impact on Share Price and Liquidity

Share Price

We consider the existence of the MD Share Schemes will not have a material effect on the Company's share price as the dilutionary impact of the MD Share Schemes is not significant.

Liquidity

Spark NZ's shares are one of the most actively traded shares on the NZX Main Board with the total volume of shares traded on the NZX Main Board in the past year equating to approximately 80% of the total shares on issue.

In our view, the MD Share Schemes will not have a positive or negative effect on the liquidity of Spark NZ's shares:

- the size of the pool of shares held by the Non-associated Shareholders will not change as a result of the MD Share Schemes
- the shares to be issued to Mr Moutter under the MD Share Schemes are subject to vesting conditions and trading restrictions.

2.9 Accounting Issues

Accounting for the MD Share Schemes shares will be governed by the requirements of New Zealand Equivalent to International Financial Reporting Standard 2 *Share-based Payment*.

The total expense to be recognised in Spark NZ's Income Statement will be the fair value of each MD Share Schemes share (using techniques consistent with generally accepted valuation methodologies for pricing financial instruments) multiplied by the number of shares which are expected to vest. The fair value of each share will be established as at the issue date. The total value of shares issued will be determined by multiplying the fair value of each share by the number of shares initially issued.

2.10 Implications of the Resolutions not being Approved

In the event that either resolution 4 or 5 in respect of the MD Share Schemes is not approved, then, under the terms of the Employment Agreement, each entitlement will be paid in cash to Mr Moutter at the equivalent value but subject to the same terms and conditions to which any equity would have been subject. The cash equivalent will be payable at the same time as any entitlements in respect of equity would have vested.

2.11 Voting For or Against the Resolutions in Respect of the MD Share Schemes

Voting for or against resolution 4 in respect of the MD Performance Equity Scheme and resolution 5 in respect of the MD Long Term Incentive Scheme is a matter for individual shareholders based on their own views as to value and future market conditions, risk profile and other factors. Shareholders will need to consider these consequences and consult their own professional adviser if appropriate.

3. Sources of Information, Reliance on Information, Disclaimer and Indemnity

3.1 Sources of Information

The statements and opinions expressed in this report are based on the following main sources of information:

- the draft notice of annual meeting
- the Spark NZ 2013, 2014 and 2015 annual reports
- the Employment Agreement
- extracts from the Board's minutes in respect of the MD Share Schemes
- the PwC Remuneration Report
- Spark NZ accounting and taxation advice in respect of the MD Share Schemes
- share price data and shareholder data from NZX Company Research.

During the course of preparing this report, we have had discussions with and / or received information from the Non-associated Directors and executive management of Spark NZ.

The Non-associated Directors have confirmed that we have been provided for the purpose of this Appraisal Report with all information relevant to the MD Share Schemes that is known to them and that all the information is true and accurate in all material aspects and is not misleading by reason of omission or otherwise.

Including this confirmation, we have obtained all the information that we believe is desirable for the purpose of preparing this Appraisal Report.

In our opinion, the information set out in this Appraisal Report is sufficient to enable the Non-associated Directors and the Non-associated Shareholders to understand all the relevant factors and to make an informed decision in respect of the MD Share Schemes.

3.2 Reliance on Information

In preparing this report we have relied upon and assumed, without independent verification, the accuracy and completeness of all information that was available from public sources and all information that was furnished to us by Spark NZ and its advisers.

We have evaluated that information through analysis, enquiry and examination for the purposes of preparing this report but we have not verified the accuracy or completeness of any such information or conducted an appraisal of any assets. We have not carried out any form of due diligence or audit on the accounting or other records of Spark NZ. We do not warrant that our enquiries would reveal any matter which an audit, due diligence review or extensive examination might disclose.

3.3 Disclaimer

We have prepared this report with care and diligence and the statements in the report are given in good faith and in the belief, on reasonable grounds, that such statements are not false or misleading. However, in no way do we guarantee or otherwise warrant that any forecasts of future profits, cash flows or financial position of Spark NZ will be achieved. Forecasts are inherently uncertain. They are predictions of future events that cannot be assured. They are based upon assumptions, many of which are beyond the control of Spark NZ and its directors and management. Actual results will vary from the forecasts and these variations may be significantly more or less favourable.

We assume no responsibility arising in any way whatsoever for errors or omissions (including responsibility to any person for negligence) for the preparation of the report to the extent that such errors or omissions result from our reasonable reliance on information provided by others or assumptions disclosed in the report or assumptions reasonably taken as implicit.

Our evaluation has been arrived at based on economic, exchange rate, market and other conditions prevailing at the date of this report. Such conditions may change significantly over relatively short periods of time. We have no obligation or undertaking to advise any person of any change in circumstances which comes to our attention after the date of this report or to review, revise or update our report.

We have had no involvement in the preparation of the notice of annual meeting issued by Spark NZ and have not verified or approved the contents of the notice of annual meeting. We do not accept any responsibility for the contents of the notice of annual meeting except for this report.

3.4 Indemnity

Spark NZ has agreed that, to the extent permitted by law, it will indemnify Simmons Corporate Finance and its directors and employees in respect of any liability suffered or incurred as a result of or in connection with the preparation of the report. This indemnity does not apply in respect of any negligence, wilful misconduct or breach of law. Spark NZ has also agreed to indemnify Simmons Corporate Finance and its directors and employees for time incurred and any costs in relation to any inquiry or proceeding initiated by any person. Where Simmons Corporate Finance or its directors and employees are found liable for or guilty of negligence, wilful misconduct or breach of law or term of reference, Simmons Corporate Finance shall reimburse such costs.

4. Qualifications and Expertise, Independence, Declarations and Consents

4.1 Qualifications and Expertise

Simmons Corporate Finance is a New Zealand owned specialist corporate finance advisory practice. It advises on mergers and acquisitions, prepares independent expert's reports and provides valuation advice.

The person in the company responsible for issuing this report is Peter Simmons, B.Com, DipBus (Finance), INFINZ (Cert).

Simmons Corporate Finance and Mr Simmons have significant experience in the independent investigation of transactions and issuing opinions on the merits and fairness of the terms and financial conditions of the transactions.

4.2 Independence

Simmons Corporate Finance does not have at the date of this report, and has not had, any shareholding in or other relationship with Spark NZ or Mr Moutter or any conflicts of interest that could affect our ability to provide an unbiased opinion in relation to this transaction.

Simmons Corporate Finance has not had any part in the formulation of the MD Share Schemes or any aspects thereof. Our sole involvement has been the preparation of this report.

Simmons Corporate Finance will receive a fixed fee for the preparation of this report. This fee is not contingent on the conclusions of this report or the outcome of the voting in respect of the MD Share Schemes. We will receive no other benefit from the preparation of this report.

4.3 Declarations

An advance draft of this report was provided to the Non-associated Directors for their comments as to the factual accuracy of the contents of the report. Changes made to the report as a result of the circulation of the draft have not changed the methodology or our conclusions.

Our terms of reference for this engagement did not contain any term which materially restricted the scope of the report.

4.4 Consents

We consent to the issuing of this report in the form and context in which it is to be included in the notice of annual meeting to be sent to Spark NZ shareholders. Neither the whole nor any part of this report, nor any reference thereto may be included in any other document without our prior written consent as to the form and context in which it appears.



Peter Simmons
Director

Simmons Corporate Finance Limited

30 September 2015