Xero Limited
2016 Annual Report

Cover image – Chow // Xero customer
Inside image – Proffer Ltd // Xero customer

Contents

Highlights

$207.1 million

Total operating revenue for year ended 31 March 2016: 67% growth

$184.0 million

Cash and cash equivalents and short-term deposits at 31 March 2016

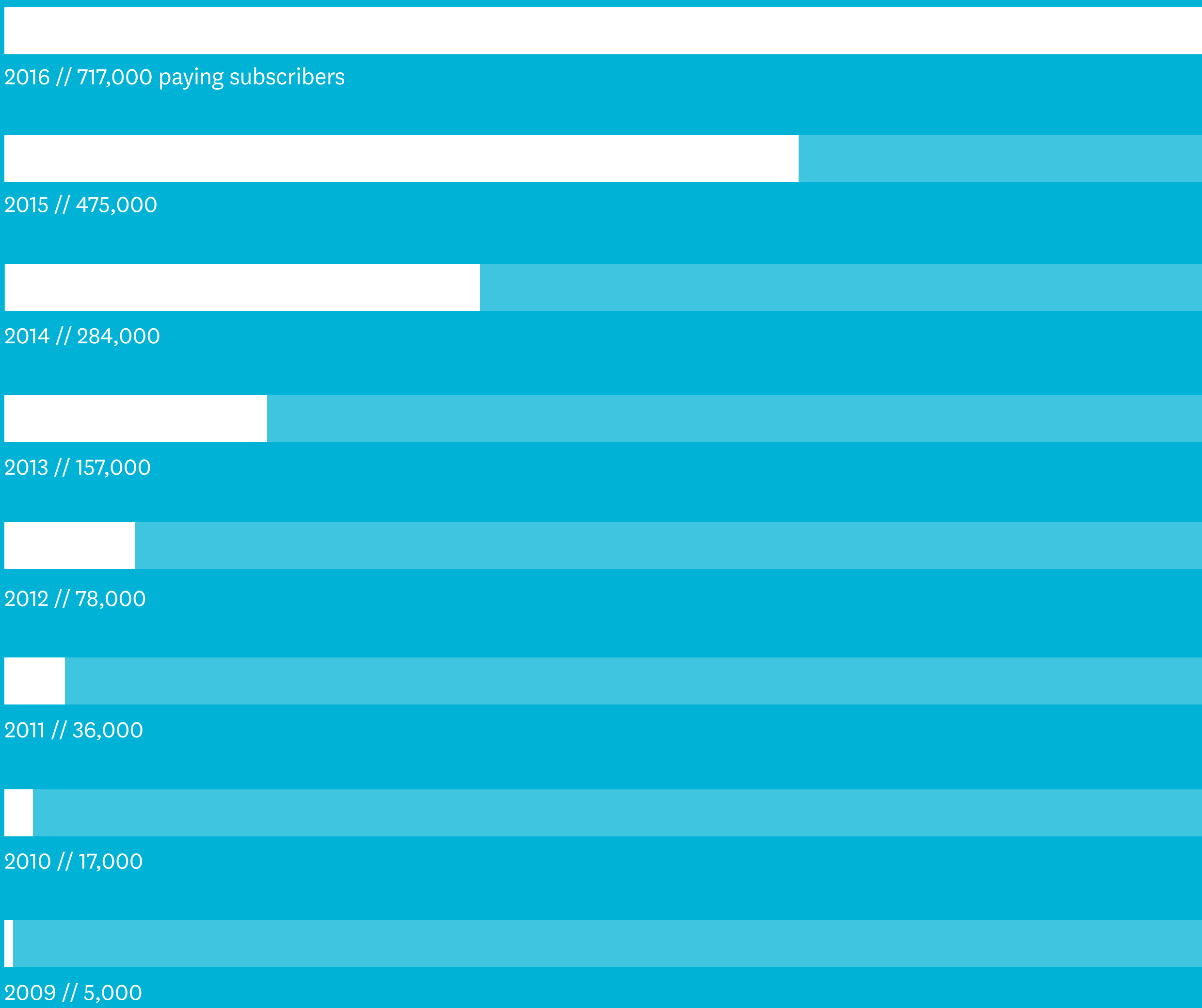
717,000

Paying subscribers at 31 March 2016

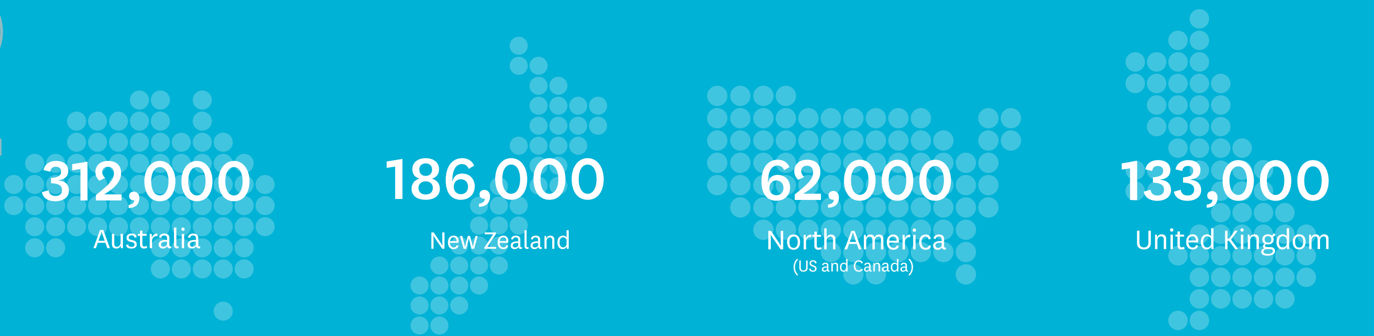
$257.9 million

Annualised committed monthly revenue at 31 March 2016

Operating revenue growth of 67% and subscriber growth of 51% in the 2016 financial year



Regional subscribers at 31 March 2016*



2014 // 109,000 2015 // 203,000

2014 // 102,000 2015 // 138,000

2014 // 18,000 2015 // 35,000

2014 // 47,000 2015 // 83,000

*Rest of World subscribers of 24,000 at 31 March 2016

Highlights

Continuing to execute on strong global growth with improving operating metrics

Strong global revenue and subscriber growth

Paid subscribers hits 717,000 globally, with 242,000 subscribers added in the 12 months to 31 March 2016

Annualised committed monthly revenue of $257.9 million, a year-on-year increase of 62%

Operating revenues of $207.1 million, an increase of 67% on the previous year

Global year-on-year revenue growth of 95% in international markets, and 57% in Australia and New Zealand

Improvement in operating metrics

Gross margin increased by six points to 76% year-on-year

Net loss of $82.5 million for the year, an increase of $12.9 million over the previous year, as Xero continues to invest in scaling its global business

EBITDA margin FY16 improved to -29% in the year from -46% in the previous year

EBITDA margin (excluding share-based compensation) improved to -22% from -38% in the previous year

Reducing cash usage[1]

Operating and investing cash usage for the second half of the year of $39.1 million, an improvement of $9.3 million from $48.5 million for the same period in the previous year

Cash usage from operating and investing activities (including FX) was $86.1 million for FY16, lower than the cash usage of $88.2 million in the previous year

Closing cash and cash equivalents and short-term deposits position of $184.0 million

1 Net movement in cash and short-term deposits excluding financing activities

Chairman and Chief Executive's Report

Dear shareholder,

Following strong subscriber growth of 242,000 to 717,000 over the past 12 months, Xero is the market-leading small business cloud accounting software in Australia, New Zealand and the United Kingdom, based on number of subscriptions. We have made good progress in the competitive United States market where the accounting industry is at an early stage in its migration to cloud technologies. Our global experience and platform investment benefits us, as the transition to cloud-based business software continues its momentum.

Our prudence in raising capital last year protected us from the correction in the global technology markets earlier this calendar year, allowing Xero to continue its global growth strategy while driving margin improvement. We have applied discipline in the deployment of capital to drive value-enhancing growth. This is most evident in the increase of $685 million in the Life-Time Value (LTV) of our subscriber base in the past year to $1.5 billion. Gross margins and EBITDA margins improved while cash usage reduced.

Based on current projections and growth plans, we have sufficient capital on hand to drive the business towards cash flow break-even. Annualised committed monthly revenue surpassed quarter of a billion and our team is focused becoming a $1 billion+ revenue generating business.

Performance highlights

The company has continued its improvement in operating metrics. We improved cash flow performance through the 12 months ended 31 March 2016. Operating revenues increased 67% year on year to $207.1 million while annualised committed monthly revenues also grew to $257.9 million, a year-on-year increase of $98.6 million, up from the year-on-year increase of $66.3 million in the previous year.

Gross margins increased six points to 76% year-on-year, while EBITDA margins improved by 17 points year on year.

We achieved cost efficiencies across the company over the past 12 months and delivered on commitments to continue investing in growth, with a greater proportion funded out of revenue.

Global growth

The success of our global growth strategy is evidenced by our cloud accounting software market leadership in Australia, New Zealand and the United Kingdom. We will continue to build in the important market of the United States and establish ourselves in other markets including South Africa, Canada, and South East Asia where we recently opened an office in Singapore to oversee our growth in the region.

"Based on current projections and growth plans, we have sufficient capital on hand to drive the business towards cash flow break-even."

"Our global focus means we are pursuing a large market of tens of millions of small businesses, most of which have yet to experience the cloud and mobility revolution enjoyed by consumers and large enterprises."

Our global focus means we are pursuing a large market of tens of millions of small businesses, most of which have yet to experience the cloud and mobility revolution enjoyed by consumers and large enterprises. By focusing on small businesses around the world, Xero has the potential to grow its customer base and market share for many years to come.

Being an accounting platform means that although we can replicate our core product globally, we must provide unique solutions for regions in which we, our small business customers and their accounting partners, operate. This work is a key task for our regional development teams globally.

It has also led to localised innovations. Not only have we developed and rolled out more than 1,200 customer-facing features and updates, but we have also produced market-specific software that helps our customers' businesses grow. For instance, we released Xero Tax in Australia, and more recently Xero TaxTouch in the United States – unique cloud-based tax solutions built specifically for their respective markets. Xero Tax has been embraced widely in Australia – in just 18 months, we have seen more than 1,400 firms adopt the platform and submit more than 1.4 million lodgements to the Australian Taxation Office. Xero TaxTouch has only been in the market since early March 2016, but we've already had positive feedback, including receiving an award at the Barlow Research's 2016 Monarch Innovation Awards for the app.

We have developed similar strategies and products in each of our core markets and will continue to do so as we build out our capabilities across the world. That's why in the United States we are pursuing a strategy of carefully managed growth as we add critical banking integrations, expand our suite of products to include simple tax filing and payroll for more states, and attract more accountants and bookkeepers.

A unique view into the small business economy

In the past 12 months, the Xero platform recorded more than $1 trillion across more than 450 million incoming and outgoing transactions. The Xero platform is providing unique and real-time insights into the importance of small business in economies that has not been available before.

In addition, cloud accounting is transitioning from distributing a software product to using software to rewire the small business economy. Enterprises are now automating their supply chains by connecting to Xero. Xero is connected to government agencies across our markets and connects small businesses across our platform.

The initial work we did connecting banks to Xero has expanded to become a financial web. By allowing small business owners to control and connect their accounting ledger to their bank, financial institution or a financial services provider, they can access services that were once primarily only offered to large enterprises, giving small businesses the ability to potentially obtain loan approvals more quickly, benefit from accessing more competitive foreign exchange rates, and more payment options.

We currently have relationships with more than 80 financial institutions around the world to help small businesses save time and administration in managing their finances and accessing services. In the future, intelligent data matching in Xero will automatically code banking transactions, making accounting even easier for small businesses.

Pace of innovation

Xero's focus on constant product and platform innovation has been core to our growth strategy. Over the past 12 months, we have delivered significant customer-facing updates and new features to our subscribers, providing them with new tools and ways of conducting their business more beautifully and efficiently.

We continued to expand our solutions ecosystem, helping small businesses connect to more than 500 solution partners who work with Xero to extend the functionality of the core accounting platform to meet customer needs and requirements.

Across the year we also expanded the ecosystem to include partnerships with major global technology companies. We integrate more closely with popular devices like the iPad and iPhone, as well as widely-used tools like Google Apps for Work, Android and Microsoft Power BI, to make collaboration between small businesses and their accounting partners easier and more efficient.

As we continue to grow our customer base, we are mindful of the need to scale our platform to provide customers with fast, secure and reliable access to their Xero data anytime, from any device. With that in mind, we are at the deployment stage of a two-year project to migrate our core cloud platform to Amazon Web Services (AWS). With our accounting engine largely complete and with such a large volume of transactions being processed on our global platform, AWS gives us access to new big data technologies such as machine learning and artificial intelligence. This provides the foundations for a new wave of innovation that will benefit Xero customers in the years to come and allow us to further differentiate our platform from those of legacy software providers.

People

Our success has been in large part thanks to the team of exceptional development, marketing, sales and support staff that contribute to Xero's success every day. We now have more than 1,450 employees across 20 offices around the world and are continuing to grow our skills and attract top talent globally.

"In the past 12 months, the Xero platform recorded more than $1 trillion across more than 450 million incoming and outgoing transactions."

"Xero has the resources and substantial revenues to continue focusing long-term on global growth and leadership while delivering the right financial results for our shareholders."

Our performance demonstrates the strength of our management team. Recent appointments to support our growth demonstrate our ability to attract top talent. Xero successfully transitioned the Chief Financial Officer role to Sankar Narayan, a seasoned CFO, public company executive, and technology leader. Andrew Lark assumed the role of Chief Marketing and Business Officer, responsible for all go-to-market functions.

We appointed Tony Stewart as Chief Data Officer, Rachael Powell as Chief People Officer, and Kirsty Godfrey-Billy as Chief Accounting Officer to boost the Xero management team in key areas. Most recently, Chief Platform Officer Duncan Ritchie resumed responsibility of the product team now that the migration to Amazon Web Services is underway.

At a local leadership level, we managed successful appointments of the Australia Managing Director, Trent Innes and New Zealand Managing Director Anna Curzon, to establish the next phase of growth in these key local markets. We also appointed Alex Campbell as Regional Managing Director to lead growth in Asia, focusing on Hong Kong, Malaysia and Singapore.

While we have grown quickly, our outstanding culture, sense of purpose and urgency remains as strong as ever.

Closing comments

This is a long journey. Though we have reached several remarkable milestones to date, in a market of tens of millions of potential customers, we have only just begun.

Xero has the resources and substantial revenues to continue focusing long-term on global growth and leadership while delivering the right financial results for our shareholders.

Our strategic priorities are to:

- continue to evolve our technology platform, extending our core accounting offering to meet the full needs of small businesses and provide new revenue opportunities
- outpace competitors through rapid product innovation, continuous improvement, and a strong customer service model
- continue the sales momentum that's driving high revenue growth in all our core markets
- grow the financial web through integrations with major banks and financial institutions
- grow our ecosystem of partners, and alliances with global brands, to create new value for both Xero and its customers.

Thank you to all our shareholders for your continued support.

Chris Liddell
Chairman

Rod Drury
Chief Executive

Management Commentary

You should read the following commentary with the consolidated financial statements and the related notes in this report. Some parts of this commentary include information regarding the plans and strategy for the business, and include forward-looking statements that involve risks and uncertainties. Actual results and the timing of certain events may differ materially from future results expressed or implied by the forward-looking statements contained in the following commentary. All numbers are presented in New Zealand dollars (NZD), except where indicated.

BUSINESS RESULTS

The information below compares the results for the year ended 31 March 2016 with the year end 31 March 2015.

Year ended 31 March	**2016 ($000s)**	**2015 ($000s)**	**change**
Subscription revenue	201,986	121,098	67%
Other operating revenue	5,074	2,922	74%
Total operating revenue	**207,060**	**124,020**	**67%**
Cost of revenue	49,881	36,708	36%
Gross profit	**157,179**	**87,312**	**80%**
Percentage of operating revenue	76%	70%	6%
Total operating expenses	**248,791**	**162,868**	**53%**
Percentage of operating revenue	*120%*	*131%*	*-11%*
Other income and foreign exchange	2,538	412	NM*
Operating deficit	**(89,074)**	**(75,144)**	**19%**
Percentage of operating revenue	-43%	-61%	18%
Net interest income	*8,122*	*7,688*	*6%*
Income tax expense	*(1,512)*	*(2,078)*	*-27%*
Net loss	**(82,464)**	**(69,534)**	**19%**
Percentage of operating revenue	*-40%*	*-56%*	*16%*

**NM stands for not meaningful.*

The growth in operating revenue was driven by subscriber growth in all markets. Average revenue per user (ARPU) held steady despite the subscriber growth. The total operating expenses and the net loss after tax have increased as Xero continues to invest in scaling its global business and delivering significant revenue growth. As a percentage of operating revenue, the net loss and all expenses for the year ended 31 March 2016 are lower than for the previous year.

EARNINGS BEFORE INTEREST, TAX, DEPRECIATION AND AMORTISATION (EBITDA)

EBITDA disclosures (which are non-GAAP financial measures) have been included, as we believe they provide useful information for readers to assist in understanding Xero's financial performance. Non-GAAP financial measures should not be viewed in isolation nor considered as substitutes for measures reported in accordance with NZ IFRS. EBITDA is calculated by adding back depreciation, amortisation, net interest income, and tax expense to net losses.

Year ended 31 March	2016 ($000s)	2015 ($000s)	change
Net loss	(82,464)	(69,534)	19%
Add back: net interest income	(8,122)	(7,688)	6%
Add back: depreciation and amortisation	29,143	17,990	62%
Add back: income tax expense	1,512	2,078	-27%
EBITDA	**(59,931)**	**(57,154)**	**5%**
Percentage of operating revenue	*-29%*	*-46%*	*17%*

EBITDA, as a percentage of operating revenue, improved compared to the year ended 31 March 2015, despite being affected by the deterioration of the NZD. The primary reason for this improvement was operating efficiencies across all expense areas.

EBITDA excluding the impact of non-cash share-based payments (a non-GAAP financial measure) is also provided as we believe it provides useful information to analyse trends in cash-based expenses.

Year ended 31 March	2016 ($000s)	2015 ($000s)	change
EBITDA	**(59,931)**	**(57,154)**	**5%**
Add back: non-cash share-based payments expenses	15,147	10,518	44%
EBITDA excluding non-cash share-based payments	**(44,784)**	**(46,636)**	**-4%**
Percentage of operating revenue	*-22%*	*-38%*	*16%*

EBITDA excluding non-cash share-based payments margins improved on a basis consistent to EBITDA margins.

OPERATING REVENUE

Subscription revenue is recurring monthly fees from customers who subscribe to Xero's online accounting software services. Within a subscription, customers also receive support services, data backup and recovery, and system updates.

Operating revenue also includes revenue from other related services such as education and the implementation of online accounting software services and conference income. However subscription revenue comprises around 98% of operating revenue.

Year ended 31 March	2016 ($000s)	2015 ($000s)	change
Subscription revenue	201,986	121,098	67%
Other operating revenue	5,074	2,922	74%
Total operating revenue	**207,060**	**124,020**	**67%**

The 67% increase in subscription revenue during the year was primarily driven by year-on-year subscriber growth of 51% from 475,000 to 717,000 at 31 March 2016. Other operating revenue increased by 74% primarily due to increased conference revenue.

OPERATING REVENUE – BY GEOGRAPHY

Year ended 31 March	2016 ($000s)	2015 ($000s)	change
Australia	96,686	58,456	65%
New Zealand	46,708	32,873	42%
Australia and New Zealand (ANZ) total	**143,394**	**91,329**	**57%**
United Kingdom	37,437	19,948	88%
North America	16,850	7,794	116%
Rest of World	9,379	4,849	93%
International total	**63,666**	**32,591**	**95%**
Corporate	-	100	NM*
Total operating revenue	**207,060**	**124,020**	**67%**

Operating revenue grew in all of Xero's geographies, with stronger growth of 95% in the earlier stage International markets compared to the more established ANZ markets.

OPERATING REVENUE – CONSTANT CURRENCY

As more than 77% of Xero's operating revenue is denominated in foreign currencies, the weakened NZD during the year affected reported revenue. On a constant currency basis, subscription and operating revenue grew by 60% compared to the year ended 31 March 2015.

Year ended 31 March	2016 ($000s)	2015 ($000s)	change
Subscription revenue – constant currency	193,393	121,098	60%
Operating revenue – constant currency	198,259	124,020	60%

This analysis is a non-GAAP financial measure, which has been provided to assist in understanding and assessing Xero's financial performance during the year, excluding the impact of foreign currency fluctuations. The constant dollar revenue translates revenue for the year ended 31 March 2016 at the effective exchange rates used for the year ended 31 March 2015.

SUBSCRIBER NUMBERS

Subscribers means each unique subscription to a Xero offered product that is purchased by an accounting partner or an end user and which is, or is available to be, deployed.

At 31 March	2016	2015	change
Australia	312,000	203,000	54%
New Zealand	186,000	138,000	35%
Australia and New Zealand (ANZ) total	**498,000**	**341,000**	**46%**
United Kingdom	133,000	83,000	60%
North America	62,000	35,000	77%
Rest of World	24,000	16,000	50%
International total	**219,000**	**134,000**	**63%**
Total paying subscribers	**717,000**	**475,000**	**51%**

Subscribers at 31 March 2016 grew by 242,000, or 51%, to 717,000 over the 12 months from 31 March 2015.

ANZ grew by 157,000 subscribers representing 46% growth in the 12 month period, evidence of strong growth in Xero's mature markets. International subscribers grew by 85,000 or 63% from the previous period.

ANNUALISED COMMITTED MONTHLY REVENUE

Annualised committed monthly revenue (ACMR) represents monthly recurring revenue at 31 March, multiplied by 12. Accordingly, it provides a twelve-month forward view of revenue, assuming any promotions have ended and other factors such as subscriber numbers, pricing and foreign exchange remain unchanged during the year.

At 31 March	2016 ($000s)	2015 ($000s)	change
ANZ	177,863	113,754	56%
International	80,062	45,584	76%
Total	**257,925**	**159,338**	**62%**

The growth in ACMR across both segments is, as previously outlined, largely driven by subscriber growth with a higher ARPU having a positive effect. ACMR at 31 March 2016 was $98.6 million or 62% higher than the prior year balance. With 76% growth in ACMR, the International markets grew faster than the more established ANZ markets. However, 56% year-on-year growth in Xero's more mature ANZ markets represents strong growth in absolute dollars, contributing nearly two thirds of Group ACMR growth.

GROSS PROFIT

Gross profit represents operating revenue less cost of revenue. Cost of revenue consists of expenses directly associated with securely hosting Xero's services, sourcing relevant customer data from banks and providing support to customers. The costs include hosting and content distribution costs, bank feed costs, personnel and related expenses (including salaries, benefits, bonuses and share-based compensation) directly associated with cloud infrastructure and customer support, contracted third-party-vendor costs, related depreciation and amortisation, and allocated overheads.

Year ended 31 March	2016 ($000s)	2015 ($000s)	change
Operating revenue	207,060	124,020	67%
Cost of revenue	(49,881)	(36,708)	36%
Gross profit	**157,179**	**87,312**	**80%**
Gross margin percentage	*76%*	*70%*	*6%*

Cost of revenue for the year ended 31 March 2016 increased by $13.2 million, or 36% to $49.9 million. The primary reasons for the change were increases in hosting costs and personnel costs related to an increased headcount in Xero's customer support teams. Operating revenue growth of 67% resulted in gross profit increasing by $69.9 million or 80%, to $157.2 million.

Cost of revenue has decreased as a percentage of operating revenue compared with the previous year due to efficiencies in the hosting and customer support teams, and reductions in bank feed costs per subscriber. This drove an improved gross margin of 76% in the current period. Cost of revenue for the second half of the year was 22% of operating revenue compared to 26% in the first half of the year, demonstrating continued improvement in gross margins throughout the year.

SALES AND MARKETING

Sales and marketing expenses consist of personnel and related expenses (including salaries, benefits, bonuses, commissions and share-based compensation) directly associated with the sales and marketing teams, the cost of educating and onboarding both partners and small business customers, and costs in the implementation of our subscription services. Other costs included are external advertising, marketing costs and promotional events including Xerocon conferences and roadshows, as well as allocated overheads.

Year ended 31 March	2016 ($000s)	2015 ($000s)	change
Sales and marketing	148,284	92,900	60%
Percentage of operating revenue	*72%*	*75%*	*-3%*

Sales and marketing costs increased by $55.4 million or 60% to $148.3 million in the year ended 31 March 2016. The majority of sales and marketing costs are incurred in acquiring new subscribers and are expensed in the period, in contrast to the associated revenue from those subscribers that is recognised over the life of the subscriber (currently 7 years on average).

As a percentage of operating revenues, sales and marketing costs decreased from 75% to 72% in the current year compared to the prior year. The second half of the year saw improvement with sales and marketing costs reducing from 76% of operating revenue in the first half of the year to 68% in the second half of the year.

PRODUCT DESIGN AND DEVELOPMENT

Product design and development costs consist primarily of personnel and related expenses (including salaries, benefits, bonuses and share-based compensation) directly associated with our product design and development employees, as well as allocated overheads.

Under New Zealand equivalents to International Financial Reporting Standards, the proportion of product design and development expenses that create a benefit in future years is capitalisable as an intangible asset and is then amortised to the Income Statement over the estimated life of the asset created. The amount amortised relating to the Xero product and platform is included as a product design and development expense.

Year ended 31 March	2016 ($000s)	2015 ($000s)	change
Total product design and development costs (including capitalised development costs)	**99,001**	**67,258**	**47%**
Percentage of operating revenue	48%	54%	-6%
Less capitalised development costs	(44,948)	(30,256)	49%
Product design and development expense excluding amortisation of capitalised development costs	**54,053**	**37,002**	**46%**
Less government grants	(3,472)	(2,946)	18%
Add amortisation of capitalised development costs	19,083	11,476	66%
Product design and development expense	**69,664**	**45,532**	**53%**
Percentage of operating revenue	*34%*	*37%*	*-3%*

Total product design and development expenses were $99.0 million in the period ended 31 March 2016, $31.7 million higher than the previous year. Of this, $44.9 million was capitalised, with the balance of $54.1 million included as an expense in the Income Statement. The amortisation of capitalised product design and development expenditure of $19.1 million was also included as an expense in the Income Statement giving a total net expense (after government grants) for the year of $69.7 million.

Total product design and development costs increased 47% due to increasing headcount and the associated personnel costs. Non-cash amortisation of previously capitalised development costs also increased due to comparably higher intangibles balances than in the prior year.

As a proportion of operating revenue, product design and development expenses decreased to 34% in the year ended 31 March 2016 from 37% for the previous year.

GENERAL AND ADMINISTRATION

General and administration expenses consist of personnel and related expenses (including salaries, benefits, bonuses and share-based compensation) for our executive, finance, billing, legal, human resources and administrative employees. It also includes legal, accounting and other professional services fees, insurance premiums, other corporate expenses and allocated overheads.

Year ended 31 March	2016 ($000s)	2015 ($000s)	change
General and administration	30,843	24,436	26%
Percentage of operating revenue	*15%*	*20%*	-5%

General and administration costs were $30.8 million for the year ended 31 March 2016, $6.4 million or 26% higher than in the previous year. The increase is primarily due to increased personnel-related costs as a result of headcount growth to support the other business functions and higher merchant bank fees from increased subscriber numbers.

General and administration costs have decreased as a proportion of operating revenue from 20% of operating revenue in the previous year to 15% in the year ended 31 March 2016.

HEADCOUNT

At 31 March	2016	2015	change
Total group	1,454	1,161	25%

Headcount increased by 293 or 25% in the year ended 31 March 2016 (taking the total headcount to 1,454) compared with a 51% increase in subscribers and 67% increase in operating revenue. The slower growth reflects the benefits of economies of scale and operating efficiencies, notwithstanding continued investment in product design and development, and the sales and marketing function.

OTHER INCOME, EXPENSES AND INTEREST

Year ended 31 March	2016 ($000s)	2015 ($000s)	change
Foreign exchange and other income			
Sublease income	758	423	79%
Other foreign exchange gains/(losses)	1,780	(11)	NM
Total foreign exchange and other income	**2,538**	**412**	**NM**
Interest			
Interest income	8,177	7,713	6%
Interest expense	(55)	(25)	120%
Net interest income	**8,122**	**7,688**	**6%**

Foreign exchange gains and losses from effective cash flow hedging relationships are now recognised in the Income Statement category being hedged (see note 2 of the financial statements for more detail).

Interest income in the period ended 31 March 2016 was $8.2 million, an increase of $0.5 million or 6% on the previous year, due to higher cash and short-term deposits balances throughout the year following the $147.2 million capital raise in March 2015. This was partially offset by lower interest rates as the New Zealand official cash rate reduced over the year.

CASH FLOWS

Year ended 31 March	2016 ($000s)	2015 ($000s)	change
Net cash provided from (used in):			
Receipts from customers	199,737	119,566	67%
Other operating cash flows	(234,507)	(158,189)	48%
Total cash flows from operating activities	**(34,770)**	**(38,623)**	**-10%**
Investing activities	(53,820)	(49,758)	8%
Total operating and investing cash flows	**(88,590)**	**(88,381)**	**0%**
Currency revaluation	2,507	207	NM
Subtotal	**(86,083)**	**(88,174)**	**-2%**

Receipts from customers increased 67% or $80.2 million to $199.7 million in line with operating revenue growth. Other net operating cash outflows increased 48% or $76.3 million, to an outflow of $234.5 million in line with increases in operating expenses.

Net cash outflows from investing activities increased by $4.1 million or 8%, as a result of continued investment in product development as well as investment in a number of internal systems to drive efficiency and scalability.

Operating and investing cash outflows remained relatively flat compared to the previous year, despite the deterioration of the NZD adversely impacting the current cash flows by $6.8 million compared with the previous period.

After revaluation of foreign currency bank accounts, operating and investing cash flows for the year ended 31 March 2016 was an outflow of $86.1 million, or $2.1 million (2%) less than the previous year, due to receipts from customers growing faster than expenses and the benefits from the revaluation of foreign currency bank accounts.

SEGMENT INFORMATION

	ANZ ($000s)	International ($000s)	Total ($000s)
Year ended 31 March 2016			
Operating revenue	143,394	63,666	207,060
Expenses	(93,982)	(104,183)	(198,165)
Other income	–	758	758
Segment contribution	**49,412**	**(39,759)**	**9,653**
Year ended 31 March 2015			
Operating revenue	91,329	32,591	123,920
Expenses	(68,328)	(61,280)	(129,608)
Other income	–	423	423
Segment contribution	**23,001**	**(28,266)**	**(5,265)**

Operating revenue is allocated to a segment depending on where the subscriber resides. Expenses include cost of revenue, sales and marketing costs incurred directly in-region, and an allocation of centrally-managed costs and overheads, such as hosting and customer support costs.

ANZ – Operating revenue for the year ended 31 March 2016 grew by 57% compared to the previous period as subscribers increased by 46%. This, along with cost efficiencies, resulted in the contribution improving as a percentage of operating revenue from 25% to 34% for the year ended 31 March 2016. The improvement was largely due to the performance in Australia, which added 109,000 subscribers in the year to finish with 312,000 paying subscribers, and revenue growth for the year of 65% to $96.7 million.

International – Operating revenue grew by 95% based on subscriber growth of 63% and a weaker NZD. Although the contribution margin improved, it reflects the investment to accelerate growth in both the United Kingdom as Xero builds brand recognition and in North America given the stage of Xero's entry into this market.

KEY SAAS METRICS

ARPU is calculated as annualised committed monthly revenue (ACMR) at 31 March divided by subscribers at that time (and divided by 12 to get a monthly view).

CAC months or months of ARPU to recover CAC (cost of acquiring subscribers) represent the number of months of revenue required to recover the cost of acquiring each new subscriber. The calculation is sales and marketing costs for the year less conference revenue (such as Xerocon) divided by new subscribers added (gross) during the same period, divided by monthly ARPU.

CMR churn is the value of committed monthly revenue (CMR) from subscribers who leave Xero in a month as a percentage of the total CMR at the start of that month. The percentage provided is the average of the monthly churn for the year. The calculation for calculating churn has been changed from subscriber churn reported previously to CMR churn, as management believes this better reflects the impact of churn on the customer base.

Lifetime value (LTV) is the gross margin expected from a subscriber over the lifetime of that subscriber. This is calculated by taking the average subscriber lifetime (1 divided by CMR churn) multiplied by ARPU multiplied by the gross margin percentage. Group LTV is calculated as the sum of the individual segments LTV multiplied by segment subscribers, divided by total Group subscribers.

Lifetime value/CAC is the ratio between the lifetime value (described above) and the cost to acquire that subscriber, e.g. the gross margin derived from a subscriber in ANZ is currently on average 9.1 times the cost of acquiring that subscriber.

The table below outlines key metrics across Xero's segments:

31 March 2016	ANZ	International	Total
ARPU ($)	29.8	30.5	30.0
CAC months	9.1	23.5	14.5
CMR churn	0.9%	1.8%	1.2%
Lifetime value per subscriber ($)	2,454	1,305	2,103
Lifetime value/CAC	9.1	1.8	4.8
31 March 2015			
ARPU ($)	27.8	28.3	28.0
CAC months	8.7	22.9	13.5
CMR churn	1.0%	2.0%	1.2%
Lifetime value per subscriber ($)	2,001	1,051	1,733
Lifetime value/CAC	8.3	1.6	4.6

ANZ – ARPU increased by 7% due to a higher portion of new and existing subscribers in New Zealand adding higher ARPU products, and due to the weakened NZD against the Australian dollar. This along with an improved gross margin led to a higher LTV.

International – ARPU increased by 8% due to a shift to higher ARPU products in the United Kingdom and due to the weakened NZD against the United States dollar and British pound. The increase in ARPU and improvement in churn led to a higher LTV in the current year.

Building a better working world

Independent Auditor's Report to the Shareholders of Xero Limited

REPORT ON THE FINANCIAL STATEMENTS

We have audited the group financial statements of Xero Limited and its subsidiaries ("the Group") on pages 19 to 42, which comprise the statement of financial position of the Group as at 31 March 2016, and the statement of comprehensive income, income statement, statement of changes in equity and statement of cash flows for the year then ended of the Group, and a summary of significant accounting policies and other explanatory information.

This report is made solely to the company's shareholders, as a body. Our audit has been undertaken so that we might state to the company's shareholders those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's shareholders as a body, for our audit work, for this report, or for the opinions we have formed.

DIRECTORS' RESPONSIBILITY FOR THE FINANCIAL STATEMENTS

The directors are responsible on behalf of the company for the preparation and fair presentation of the financial statements in accordance with New Zealand Equivalents to International Financial Reporting Standards and International Financial Reporting Standards, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

AUDITOR'S RESPONSIBILITY

Our responsibility is to express an opinion on the financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing (New Zealand). These auditing standards require that we comply with relevant ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we have considered the internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates, as well as evaluating the overall presentation of the financial statements.

We believe we have obtained sufficient and appropriate audit evidence to provide a basis for our audit opinion.

Other than in our capacity as auditor and providing remuneration market benchmark data and tax compliance services we have no relationship with, or interest in, the Group. Ernst & Young, its Partners and employees may deal with the Group on normal terms within the ordinary course of trading activities of the business of the Group.

OPINION

In our opinion, the financial statements on pages 19 to 42 present fairly, in all material respects, the financial position of the Group as at 31 March 2016 and the financial performance and cash flows of the Group for the year then ended in accordance with New Zealand Equivalents to International Financial Reporting Standards and International Financial Reporting Standards.

Ernst & Young

ERNST & YOUNG

12 May 2016
Wellington

Financial Statements

Income statement

	Notes	Year ended 31 March 2016 ($000s)	Year ended 31 March 2015 ($000s)
Subscription revenue		201,986	121,098
Other operating revenue		5,074	2,922
Total operating revenue	**4**	**207,060**	**124,020**
Cost of revenue	6	49,881	36,708
Gross profit		**157,179**	**87,312**
Operating expenses			
Sales and marketing		148,284	92,900
Product design and development		69,664	45,532
General and administration		30,843	24,436
Total operating expenses	**6**	**248,791**	**162,868**
Foreign exchange gains/(losses)		1,780	(11)
Other income		758	423
Operating deficit		**(89,074)**	**(75,144)**
Net interest income	5	8,122	7,688
Net loss before tax		**(80,952)**	**(67,456)**
Income tax expense	7	(1,512)	(2,078)
Net loss		**(82,464)**	**(69,534)**
Earnings per share			
Basic and diluted loss per share	8	($0.60)	($0.55)

Statement of comprehensive income

	Note	Year ended 31 March 2016 ($000s)	Year ended 31 March 2015 ($000s)
Net loss		(82,464)	(69,534)
Other comprehensive income*			
Movement in cash flow hedges (net of tax)	18	(5,800)	2,175
Translation of international subsidiaries		2,079	(646)
Total other comprehensive income/(loss) for the year		**(3,721)**	**1,529**
Total comprehensive loss for the year		**(86,185)**	**(68,005)**

** Items of other comprehensive income may be reclassified to the Income Statement*

The accompanying notes form an integral part of these financial statements

Statement of changes in equity

	Notes	Share capital ($000s)	Treasury shares ($000s)	Share-based payment reserve ($000s)	Accumulated losses ($000s)	Foreign currency translation reserve ($000s)	Cash flow hedge reserve ($000s)	Total equity ($000s)
Balance at 1 April 2015		**504,570**	**(12,565)**	**7,705**	**(155,474)**	**(758)**	**2,175**	**345,653**
Net loss		–	–	–	(82,464)	–	–	(82,464)
Other comprehensive loss		–	–	–	–	2,079	(5,800)	(3,721)
Total comprehensive loss		**–**	**–**	**–**	**(82,464)**	**2,079**	**(5,800)**	**(86,185)**
Transactions with owners:								
Share-based payments – employee restricted share plan	20	9,443	(254)	620	–	–	–	9,809
Share-based payments – restricted stock units	20	1,242	–	5,434	–	–	–	6,676
Share-based director fees and options	20	70	–	844	–	–	–	914
Share-based payments – employee share options	20	–	–	548	–	–	–	548
Exercising of director share options	14	209	–	(43)	–	–	–	166
Exercising of employee share options	14	631	–	(96)	–	–	–	535
Share-based payments – employee schemes arising on acquisition		–	–	973	–	–	–	973
Balance at 31 March 2016		**516,165**	**(12,819)**	**15,985**	**(237,938)**	**1,321**	**(3,625)**	**279,089**
Balance at 1 April 2014		**341,436**	**(5,128)**	**4,682**	**(85,940)**	**(112)**	**–**	**254,938**
Net loss		–	–	–	(69,534)	–	–	(69,534)
Other comprehensive income		–	–	–	–	(646)	2,175	1,529
Total comprehensive loss		**–**	**–**	**–**	**(69,534)**	**(646)**	**2,175**	**(68,005)**
Transactions with owners:								
Issue of shares (net of issue costs)		144,275	–	–	–	–	–	144,275
Share-based payments – employee restricted share plan	20	13,033	(7,208)	1,650	–	–	–	7,475
Share-based payments – restricted stock units	20	885	–	652	–	–	–	1,537
Share-based director fees and options	20	35	–	1,346	–	–	–	1,381
Share-based payments – employee share options	20	–	–	475	–	–	–	475
Exercising of director share options	14	443	–	(112)	–	–	–	331
Exercising of employee share options	14	476	–	(99)	–	–	–	377
Issue of shares – purchase of Monchilla, Inc.		3,987	(1,993)	–	–	–	–	1,994
Share-based payments – employee schemes arising on acquisition		–	1,764	(889)	–	–	–	875
Balance at 31 March 2015		**504,570**	**(12,565)**	**7,705**	**(155,474)**	**(758)**	**2,175**	**345,653**

The accompanying notes form an integral part of these financial statements

Statement of financial position

	Notes	At 31 March 2016 ($000s)	2015 ($000s)
Assets			
Current assets			
Cash and cash equivalents		39,024	58,866
Short-term deposits		145,000	210,000
Trade and other receivables	9	27,098	21,499
Short-term derivative assets	18	358	3,151
Total current assets		**211,480**	**293,516**
Non-current assets			
Property, plant and equipment	10	15,462	16,631
Intangible assets	11	97,779	65,112
Deferred tax asset	7	1,376	1,427
Other receivables		2,004	1,712
Total non-current assets		**116,621**	**84,882**
Total assets		**328,101**	**378,398**
Liabilities			
Current liabilities			
Trade and other payables	12	21,634	13,937
Employee entitlements		20,783	14,040
Income tax payable	7	311	2,218
Short-term provisions	13	63	26
Short-term derivative liabilities	18	3,983	130
Total current liabilities		**46,774**	**30,351**
Non-current liabilities			
Deferred tax liability	7	755	1,453
Long-term provisions	13	972	828
Other long-term liabilities		511	113
Total non-current liabilities		**2,238**	**2,394**
Total liabilities		**49,012**	**32,745**
Equity			
Share capital	14	503,346	492,005
Share-based payment reserve	20	15,985	7,705
Accumulated losses		(237,938)	(155,474)
Foreign currency translation reserve		1,321	(758)
Cash flow hedge reserve	18	(3,625)	2,175
Total equity		**279,089**	**345,653**
Total liabilities and shareholders' equity		**328,101**	**378,398**

The accompanying notes form an integral part of these financial statements

Statement of cash flows

	Note	Year ended 31 March 2016 ($000s)	2015 ($000s)
Operating activities			
Receipts from customers		199,737	119,566
Other income		4,144	2,580
Interest received		9,852	7,950
Payments to suppliers and employees		(245,288)	(166,724)
Income tax paid		(3,215)	(1,995)
Net cash flows from operating activities	15	**(34,770)**	**(38,623)**
Investing activities			
Purchase of property, plant and equipment		(4,749)	(10,315)
Capitalised development costs		(47,749)	(32,994)
Business acquisitions		-	(5,349)
Other intangible assets		(1,192)	(174)
Rental bonds		(130)	(926)
Net cash flows from investing activities		**(53,820)**	**(49,758)**
Financing activities			
Exercising of share options		701	709
Share issue		–	147,200
Repayment of management loan		540	2,090
Cost of share issue		–	(2,845)
Payments for short-term deposits		(145,000)	(418,000)
Proceeds from short-term deposits		210,000	403,000
Net cash flows from financing activities		**66,241**	**132,154**
Net increase/(decrease) in cash and cash equivalents		**(22,349)**	**43,773**
Foreign currency translation adjustment		2,507	207
Cash and cash equivalents at the beginning of the year		**58,866**	**14,886**
Cash and cash equivalents at the end of the year		**39,024**	**58,866**

The accompanying notes form an integral part of these financial statements

Notes to the financial statements

1. REPORTING ENTITY AND STATUTORY BASE

Xero Limited is a company registered under the Companies Act 1993 and is listed on the New Zealand Stock Exchange (NZX) and the Australian Securities Exchange (ASX). The Company is an FMC reporting entity under Part 7 of the Financial Markets Conduct Act 2013. The financial statements of the Group have been prepared in accordance with the requirements of Part 7 of the Financial Markets Conduct Act 2013 and the NZX Main Board Listing Rules.

In accordance with the Financial Markets Conduct Act 2013, because Group financial statements are prepared and presented for Xero Limited and its subsidiaries, separate financial statements for Xero Limited are not required and therefore have not been presented.

The consolidated financial statements of the Group for the year ended 31 March 2016 were authorised for issue in accordance with a resolution of the Directors on 12 May 2016.

The Group's principal activity is the provision of a platform for online accounting and business services to small businesses and their advisors.

2. BASIS OF ACCOUNTING

(a) Basis of preparation The consolidated financial statements of the Group have been prepared in accordance with Generally Accepted Accounting Practice in New Zealand (NZ GAAP). The Group is a for-profit entity for the purposes of complying with NZ GAAP. The consolidated financial statements comply with New Zealand equivalents to International Financial Reporting Standards (NZ IFRS), other New Zealand accounting standards and relevant authoritative notices that are applicable to entities that apply NZ IFRS. The consolidated financial statements also comply with International Financial Reporting Standards.

Other than where described below or in the notes, the consolidated financial statements have been prepared using the historical cost convention.

The consolidated financial statements are presented in New Zealand dollars ($) (NZD) (the 'presentation currency'). Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the 'functional currency').

(b) Changes in accounting policies and disclosures Apart from the changes noted below, the accounting policies adopted are consistent with those of the previous year.

During the year, the Group's operating segments were redefined based on the way in which the Global Executive Team reviews performance. The change results in two reportable segments, namely Australia and New Zealand (ANZ) and International.

Grant income previously recorded in other income is now recognised contra product design and development expenses in order to more appropriately reflect the nature of the grant income. Comparative amounts in the consolidated Income Statement were reclassified for consistency, which resulted in $2.9 million being reclassified from other income to product design and development expenses for the year ended 31 March 2015.

Hedging gains and losses previously recorded as part of other income is now allocated and recognised within the operating revenue or expense line item to which the underlying hedged item relates. Comparative amounts in the consolidated Income Statement were reclassified for consistency, which resulted in an increase to subscription revenue of $170,000, and decreases to cost of revenue, sales and marketing, product design and development, and general and administration expense categories of $695,000, $578,000, $481,000 and $112,000 respectively.

Certain other comparative information has also been reclassified to conform with the current period's presentation.

(c) Standards or interpretations issued but not yet effective and relevant to the Group The International Accounting Standards Board has issued a number of standards, amendments and interpretations which are not yet effective and which may have an impact on the Group's financial statements. These are detailed below. The Group has not applied these in preparing these financial statements and will apply each standard in the period in which it becomes mandatory:

- **(a) NZ IFRS 9 – Financial Instruments – Classification and Measurement** This standard addresses the classification, measurement and de-recognition of financial assets, financial liabilities, impairment of financial assets and hedge accounting, and will be effective for the year ended 31 March 2019.
- **(b) NZ IFRS 15 – Revenue from Contracts with Customers** This standard establishes the framework for revenue recognition, and will be effective for the year ended 31 March 2019.
- **(c) NZ IFRS 16 – Leases** This standard requires a lessee to recognise a lease liability reflecting the future lease payments and a 'right-of-use asset' for substantively all lease contracts, and will be effective for the year ended 31 March 2020.

The Group has not yet assessed the potential impact of the above standards.

(d) Critical accounting estimates In applying the Group's accounting policies, management continually evaluates judgements, estimates and assumptions based on experience and other factors, including expectations of future events that may have an impact on the Group. All judgements, estimates and assumptions made are believed to be reasonable based on the most current set of circumstances available to the Group. Actual results may differ from the judgements, estimates and assumptions.

The significant judgements, estimates and assumptions made by management in the preparation of these financial statements are outlined below.

Deferred tax assets The Group recognises a deferred tax asset in relation to tax losses, only to the extent of the Group's deferred tax liabilities. The Group has not recognised a deferred tax asset in respect of additional losses or other temporary differences given the uncertainty of the timing of profitability and the requirement for ownership continuity. Deferred tax assets and deferred tax liabilities are recognised in the subsidiaries in respect of temporary differences; assets are only recognised to the extent that it is probable the assets will be utilised.

Capitalised development costs The Group capitalises a proportion of employee costs related to software development. The Group regularly reviews the carrying value of capitalised development costs to ensure they are not impaired. The development costs are amortised over three to five years, the expected useful life of the assets, with limited exceptions to this for assets specifically identified as having shorter useful lives.

At 31 March 2016, if capitalisation rates had been 10% higher/lower with all other variables held constant, the impact on operational expenses would have been $9.9 million lower/higher.

3. SEGMENT INFORMATION

The Group operates in one business segment, providing online solutions for small businesses and their advisors.

Xero has two operating segments. These segments have been determined based on reports reviewed by the Global Executive Team (the chief operating decision-maker). Segment operating expenses represent sales and marketing costs and service delivery costs, including both in-country costs and an allocation of centrally managed costs.

Segment contribution

	ANZ ($000s)	International ($000s)	Total ($000s)
Year ended 31 March 2016			
Operating revenue	143,394	63,666	207,060
Expenses	(93,982)	(104,183)	(198,165)
Other income	–	758	758
Segment contribution	**49,412**	**(39,759)**	**9,653**
Year ended 31 March 2015			
Operating revenue	91,329	32,591	123,920
Expenses	(68,328)	(61,280)	(129,608)
Other income	–	423	423
Segment contribution	**23,001**	**(28,266)**	**(5,265)**

Reconciliation from segment result to consolidated operating revenue

Year ended 31 March 2016	2016 ($000s)	2015 ($000s)
Segment revenue	207,060	123,920
Corporate revenue	–	100
Total operating revenue	**207,060**	**124,020**

Reconciliation from segment result to consolidated net loss before income tax

Year ended 31 March 2016	2016 ($000s)	2015 ($000s)
Segment contribution	9,653	(5,265)
Corporate revenue	–	100
Product design and development	(69,664)	(45,532)
General and administration	(30,843)	(24,436)
Foreign exchange gains/(losses)	1,780	(11)
Net interest income	8,122	7,688
Net loss before tax	**(80,952)**	**(67,456)**

At 31 March 2016 $104.0 million, or 92%, of the Group's property, plant and equipment and intangible assets were domiciled in New Zealand (2015: $71.7 million).

Depreciation and amortisation by segment

Year ended 31 March	2016 ($000s)	2015 ($000s)
ANZ	1,984	1,667
International	3,263	1,136
Corporate (not allocated to a segment)	23,896	15,187
Total	**29,143**	**17,990**

Employee entitlements: share-based payments by segment

Year ended 31 March	2016 ($000s)	2015 ($000s)
ANZ	3,666	2,404
International	4,380	1,538
Corporate (not allocated to a segment)	6,691	5,230
Total	**14,737**	**9,172**

4. REVENUE

Subscription revenue Subscription revenue comprises the recurring monthly fees from subscribers to Xero's online accounting software services. Subscribers are invoiced monthly in arrears, with no set contractual term. Revenue is recognised as the services are provided to the subscribers. Unbilled revenue at year end is recognised in the Statement of Financial Position as accrued income and included within trade and other receivables.

Other operating revenue Other operating revenue comprises revenue from related services such as education and implementation of the online accounting software services, along with conference income. Revenue is recognised as the services are provided to customers.

Revenue by geographic region

Year ended 31 March	2016 ($000s)	2015 ($000s)
Australia	96,686	58,456
New Zealand	46,708	32,873
United Kingdom	37,437	19,948
North America	16,850	7,794
Rest of World	9,379	4,849
Corporate	–	100
Total	**207,060**	**124,020**

5. NET INTEREST INCOME

Interest income is recognised as it is accrued using the effective interest method. The effective interest method calculates the amortised cost of the financial asset and allocates the interest income over its expected life.

Year ended 31 March	2016 ($000s)	2015 ($000s)
Interest income – cash and short-term deposits	8,172	7,616
Interest income – loans to key management personnel	5	97
Interest expense	(55)	(25)
Total net interest income	**8,122**	**7,688**

6. EXPENSES

Sales tax The Income Statement and the Statement of Cash Flows have been prepared so that all components are stated exclusive of sales tax, except where sales tax is not recoverable. All items in the Statement of Financial Position are stated net of sales tax with the exception of receivables and payables, which include the sales tax invoiced. Sales tax includes Goods and Services Tax, and Value Added Tax, where applicable.

Overhead allocation The presentation of the Income Statement by function requires certain overhead costs to be allocated to functions. These allocations require management to apply judgement. Facilities, internal information technology costs, and depreciation and amortisation not relating to product software development have been allocated to each function on a headcount basis. Recruitment costs have been allocated according to the number of employees hired in each function during the period. The amortisation of product-related software development is included in product design and development.

Year ended 31 March	2016 ($000s)	2015 ($000s)
Cost of revenue and operating expenses		
Employee entitlements	159,210	106,153
Employee entitlements – share-based payments	18,563	15,263
Employee entitlements capitalised	(42,690)	(28,504)
IT infrastructure costs	18,277	10,909
Advertising and marketing	53,781	29,683
Consulting and subcontracting	13,082	7,138
Rental costs	9,909	7,425
Travel-related costs	6,453	5,609
Communication and office administration	4,123	3,589
Staff recruitment	2,064	2,565
Superannuation costs	5,085	3,803
Computer equipment and software	4,547	2,970
Directors' fees	796	515
Auditors remuneration	460	627
Other operating expenses	15,869	13,841
Total cost of revenue and operating expenses excl. depreciation and amortisation*	**269,529**	**181,586**

** Includes grant income of $3.5 million (2015: $2.9 million)*

Depreciation and amortisation	2016 ($000s)	2015 ($000s)
Relating to:		
Amortisation of development costs	22,019	12,947
Amortisation of other intangible assets	698	346
Depreciation of property, plant and equipment	6,426	4,697
Total depreciation and amortisation	**29,143**	**17,990**
Total cost of revenue and operating expenses	**298,672**	**199,576**

Depreciation and amortisation included in function expenses as follows:	2016 ($000s)	2015 ($000s)
Cost of revenue	2,348	1,279
Sales and marketing	2,898	1,982
Product design and development	23,145	14,284
General and administration	752	445
Total depreciation and amortisation	**29,143**	**17,990**

Auditor's remuneration

Year ended 31 March	2016 ($000s)	2015 ($000s)
Audit and review of financial statements – EY	205	–
Taxation services – EY	42	–
Other services* – EY	15	–
Audit and review of financial statements – PwC	–	205
Other assurance services** – PwC	198	354
Taxation services – PwC	–	27
Other services*** – PwC	–	41
Total fees paid to auditors	**460**	**627**

** Services relate to provision of remuneration market data*
*** Services relate to assurance services in relation to the preparation of US GAAP-compliant financial statements, audit of the Company's share register and compliance engagement in respect of a grant application*
**** Services relating to global mobility, and other services in respect of IT change management and disaster recovery advice*

7. CURRENT AND DEFERRED INCOME TAX

Tax expense comprises current and deferred tax. Income tax is recognised in the Income Statement except when it relates to items recognised directly in other comprehensive income, (in which case the income tax is recognised in other comprehensive income). Income tax is based on tax rates and regulations enacted, or substantially enacted, in the jurisdictions in which the entity operates.

Deferred tax is recognised in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The amount of deferred tax is based on the expected manner of realisation of the carrying amount of assets and liabilities, using tax rates enacted or substantially enacted at the end of the reporting period.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised.

Current income tax The tax on the Group's loss before tax differs from the theoretical amount that would arise using the weighted average tax rate applicable to the profits or loss of the consolidated entities as follows:

Year ended 31 March	2016 ($000s)	2015 ($000s)
Accounting loss before income tax	(80,952)	(67,456)
At the statutory income tax rate of 28%	(22,667)	(18,888)
Non-deductible expenditure	1,317	723
Prior period adjustment	(490)	467
Impact of R&D credit claims made in current year	(510)	–
Tax rate variance of subsidiaries	166	416
Total tax losses not recognised	23,696	19,360
Income tax expense	**1,512**	**2,078**
Comprising:		
Income tax payable	2,788	3,589
Prior period adjustment	(490)	467
Impact of R&D credit claims made in current year	(510)	–
Deferred tax	(1,228)	(1,132)
Tax losses utilised	846	(846)
Effect of changes in foreign currency	106	–
Income tax expense	**1,512**	**2,078**

Income tax payable

At 31 March	2016 ($000s)	2015 ($000s)
Opening balance	2,218	732
Prior period adjustment	(1,165)	(209)
Impact of R&D credit claims processed in current year	(510)	–
Income tax liability for the year	2,788	3,589
Income tax paid	(3,215)	(1,995)
Effects of changes in foreign currency	195	101
Current tax payable	**311**	**2,218**

Deferred income tax

The analysis of deferred tax assets and deferred tax liabilities is as follows:

	Derivatives ($000s)	Provisions & employee benefits ($000s)	Tax depreciation ($000s)	Tax losses ($000s)	Total ($000s)
Year ended 31 March 2016					
Deferred tax asset balances:					
At 1 April 2015	–	1,247	180	–	1,427
Prior period adjustment	–	(882)	(191)	–	(1,073)
Charged to Income Statement	–	1,231	(302)	–	929
Foreign currency adjustment	–	93	–	–	93
At 31 March 2016	**–**	**1,689**	**(313)**	**–**	**1,376**
Deferred tax liability balances:					
At 1 April 2015	(846)	1,691	(4,650)	2,352	(1,453)
Prior period adjustment	–	99	77	223	399
Charged to Income Statement	–	438	(2,419)	2,280	299
Charged to other comprehensive income	1,861	–	–	(1,015)	846
Tax losses utilised	–	–	–	(846)	(846)
At 31 March 2016	**1,015**	**2,228**	**(6,992)**	**2,994**	**(755)**
Year ended 31 March 2015					
Deferred tax asset balances:					
At 1 April 2014	–	1,089	(1,497)	894	486
Prior period adjustment	–	(301)	(98)	(217)	(616)
Charged to Income Statement	–	460	1,774	(677)	1,557
Foreign currency adjustment	–	(1)	1	–	–
At 31 March 2015	**–**	**1,247**	**180**	**–**	**1,427**
Deferred tax liability balances:					
At 1 April 2014	–	–	–	–	–
Charged to Income Statement	–	1,514	(3,445)	1,506	(425)
Charged to other comprehensive income	(846)	–	–	–	(846)
Tax losses utilised	–	–	–	846	846
Acquisition of Monchilla. Inc	–	–	(1,056)	–	(1,056)
Foreign currency adjustment	–	177	(149)	–	28
At 31 March 2015	**(846)**	**1,691**	**(4,650)**	**2,352**	**(1,453)**

The Group's deferred tax asset and deferred tax liability are expected to be recovered by $0.3 million and $0.3 million respectively within the next 12 months. Deferred tax assets and liabilities have been offset where the balances are due to/receivable from the same counterparties. Deferred income tax assets are recognised for carried forward tax losses to the extent of the Company's deferred tax liabilities. The Company has unrecognised New Zealand tax losses available to carry forward of $241,082,000 (2015: $144,945,000) subject to shareholder continuity being maintained as required by New Zealand tax legislation.

8. EARNINGS PER SHARE

The Group presents basic and diluted earnings per share (EPS) data for its ordinary shares.

Basic EPS is calculated by dividing the net loss attributable to ordinary shareholders of the Company by the weighted average number of ordinary shares on issue during the year, excluding shares purchased and held as treasury shares.

Diluted EPS is determined by adjusting the net loss attributable to ordinary shareholders and the weighted average number of ordinary shares on issue for the effects of all dilutive potential ordinary shares, which comprise treasury shares, options and Restricted Stock Units (RSUs) granted to employees and Directors. Potential ordinary shares are treated as dilutive when, and only when, their conversion to ordinary shares would decrease EPS or increase the loss per share.

Year ended 31 March	2016 (000s)*	2015 (000s)*
Weighted average number of issued ordinary shares	136,429	127,323
Net loss after tax	(82,464)	(69,534)
Basic and diluted loss per share (in New Zealand dollars)	**($0.60)**	**($0.55)**

**Except for per share amounts*

9. TRADE AND OTHER RECEIVABLES

Trade and other receivables are initially recognised at the fair value of the amounts to be received, plus transaction costs (if any). They are subsequently measured at amortised cost (using the effective interest method) less impairment losses.

At 31 March	2016 ($000s)	2015 ($000s)
Trade receivables	8,708	5,723
Provision for doubtful debts	(134)	(117)
Accrued income	9,719	5,526
Prepayments	6,463	5,752
Interest receivable	1,316	2,919
Government grant receivable	964	836
Rental bonds and other deposits	62	248
Loans to key management	–	612
Total current trade and other receivables	**27,098**	**21,499**

Trade receivables are related primarily to the monthly subscriptions charged for the Xero software. Subscriptions are charged monthly in arrears and paid by direct debit. At 31 March 2016 trade receivables of the Group of $367,000 were past due and are considered partially impaired (2015: $137,000).

10. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment are stated at historical cost less depreciation.

Depreciation is charged on a straight-line basis to allocate the differences between the original cost and the residual values over the estimated useful lives, as follows:

Leasehold improvements	Term of lease
Motor vehicles	5 years
Computer equipment	2-3 years
Furniture and equipment	2-7 years

The assets' residual values and useful lives are reviewed and adjusted if appropriate at each balance date. If an asset's carrying amount is greater than its estimated recoverable amount, the carrying amount is written down immediately to its recoverable amount.

	Leasehold improvements ($000s)	Motor vehicles ($000s)	Computer equipment ($000s)	Furniture and equipment ($000s)	Total ($000s)
Cost					
Balance at 1 April 2015	9,738	212	6,286	7,899	24,135
Additions	1,778	–	1,771	1,045	4,594
Disposals	(225)	–	(2,105)	(381)	(2,711)
Foreign exchange adjustment	358	2	231	301	892
Balance at 31 March 2016	**11,649**	**214**	**6,183**	**8,864**	**26,910**
Accumulated depreciation					
Balance at 1 April 2015	2,541	118	2,950	1,895	7,504
Depreciation expense	2,300	32	2,371	1,723	6,426
Disposals	(222)	–	(2,037)	(374)	(2,633)
Foreign exchange adjustment	66	2	67	16	151
Balance at 31 March 2016	**4,685**	**152**	**3,351**	**3,260**	**11,448**
Net book value at 31 March 2016	**6,964**	**62**	**2,832**	**5,604**	**15,462**
Cost					
Balance at 1 April 2014	5,739	187	3,395	3,922	13,243
Additions	4,530	25	3,038	3,874	11,467
Disposals	(540)	–	(233)	(23)	(796)
Foreign exchange adjustment	9	–	86	126	221
Balance at 31 March 2015	**9,738**	**212**	**6,286**	**7,899**	**24,135**
Accumulated depreciation					
Balance at 1 April 2014	1,224	84	1,295	784	3,387
Depreciation expense	1,675	34	1,866	1,122	4,697
Disposals	(351)	–	(228)	(18)	(597)
Foreign exchange adjustment	(7)	–	17	7	17
Balance at 31 March 2015	**2,541**	**118**	**2,950**	**1,895**	**7,504**
Net book value at 31 March 2015	**7,197**	**94**	**3,336**	**6,004**	**16,631**

11. INTANGIBLE ASSETS

Costs that are directly associated with the development of software are recognised as intangible assets where the following criteria are met:

- it is technically feasible to complete the software product so that it will be available for use;
- management intends to complete the software product and use or sell it;
- there is an ability to use or sell the software product;
- it can be demonstrated how the software product will generate probable future economic benefits;
- adequate technical, financial and other resources to complete the development and to use or sell the software product are available; and
- the expenditure attributable to the software product during its development can be reliably measured.

Software development costs that meet the above criteria are capitalised. Other development expenditure that does not meet the above criteria is recognised as an expense as incurred. Development costs previously recognised as expenses are not recognised as assets in a subsequent period. Software development costs recognised as assets are amortised over their estimated useful lives.

Other intangible assets acquired are initially measured at cost. Internally generated assets, excluding capitalised development costs, are not capitalised and are recognised in the Income Statement when the expenditure is incurred.

With the exception of goodwill, the useful lives of the Group's intangible assets are assessed to be finite. Assets with finite lives are amortised over their useful lives and tested for impairment whenever there are indications that the assets may be impaired.

Amortisation is recognised in the Income Statement on a straight-line basis over the estimated useful life of the intangible asset, from the date it is available for use. The estimated useful lives are as follows:

Capitalised software development costs	3-5 years
Software licence costs	1-3 years
Patents, domains and trademark costs	10 years

Research costs and costs associated with maintenance are recognised as an expense as incurred.

Goodwill Goodwill represents the excess of purchase consideration over the fair value of net assets acquired at the time of acquisition of a business or shares in a subsidiary. Goodwill is allocated to cash-generating units (CGUs), which are the lowest level of assets for which separately identifiable cash flows can be attributed.

Impairment considerations At each reporting date, the Group assesses whether there is any indication that an asset may be impaired. Where an indicator of impairment exists, the Group makes a formal estimate of the recoverable amount. Where the carrying value of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount.

The recoverable amount is the greater of fair value less costs to sell or the asset's value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows.

Goodwill is tested at least annually for impairment, or whenever indicators of impairment exist.

An impairment loss is recorded if its recoverable amount is less than its carrying amount. The recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate.

	Software development* ($000s)	Software licences ($000s)	Other intangible assets ($000s)	Goodwill ($000s)	Total ($000s)
Cost					
Balance at 1 April 2015	85,918	350	816	5,352	92,436
Additions**	52,877	2,653	159	–	55,689
Disposals	(306)	(196)	–	–	(502)
Balance at 31 March 2016	**138,489**	**2,807**	**975**	**5,352**	**147,623**
Accumulated amortisation					
Balance at 1 April 2015	26,821	223	280	–	27,324
Amortisation	22,019	389	309	–	22,717
Disposals	–	(197)	–	–	(197)
Balance at 31 March 2016	**48,840**	**415**	**589**	**–**	**49,844**
Net book value at 31 March 2016	**89,649**	**2,392**	**386**	**5,352**	**97,779**
Cost					
Balance at 1 April 2014	48,443	276	204	–	48,923
Additions**	34,883	168	158	–	35,209
Acquisitions	2,592	–	454	5,352	8,398
Disposals	–	(94)	–	–	(94)
Balance at 31 March 2015	**85,918**	**350**	**816**	**5,352**	**92,436**
Accumulated amortisation					
Balance at 1 April 2014	13,874	158	63	–	14,095
Amortisation	12,947	129	217	–	13,293
Disposals	–	(64)	–	–	(64)
Balance at 31 March 2015	**26,821**	**223**	**280**	**–**	**27,324**
Net book value at 31 March 2015	**59,097**	**127**	**536**	**5,352**	**65,112**

** Included in software development are projects in progress with a year end balance of $2.0 million (2015: $4.2 million)*
*** Includes $8.6 million of externally purchased assets (2015: $6.4)*

Goodwill impairment testing Goodwill acquired in a business combination is allocated to the cash generating unit (CGU) that benefits from the synergies of the acquisition. Xero's goodwill relates to the acquisition of Monchilla, Inc. and has been allocated to the North American market.

The recoverable amount of the North American market was calculated on the basis of value in use using a discounted cash flow model. Future cash flows were projected for ten years, with key assumptions being CGU earnings and capital expenditure for the CGU based on the market's forecasts of expected performance.

A terminal growth rate of 2.5% (2015: 3%) was applied and a pre-tax discount rate of 12% was utilised (2015: 20%). The terminal growth rate is determined based on the long-term anticipated growth rate of the business. The forecast financial information is based on both past experience and future expectations of CGU performance. The major inputs and assumptions used in performing an impairment assessment that require judgement include revenue forecasts, operating cost projections, customer numbers and churn, discount rates, growth rates and future technology paths.

During the year ended 31 March 2016 no impairment arose as a result of the review of goodwill. The recoverable amount of the North American CGU is greater than the carrying amount and, based on sensitivity analysis performed, no foreseeable changes in the assumptions would cause the carrying amount of the CGU to exceed its recoverable amount.

12. TRADE AND OTHER PAYABLES

The Group recognises trade and other payables initially at fair value and subsequently at amortised cost using the effective interest method. The amounts are unsecured, non-interest bearing and usually paid within 45 days of recognition.

At 31 March	2016 ($000s)	2015 ($000s)
Trade payables	9,609	5,700
Accrued expenses	8,685	6,414
Income in advance	789	965
Sales tax payable	2,551	858
Total current trade and other payables	**21,634**	**13,937**

13. PROVISIONS

Provisions are recognised when the Group has a present legal or constructive obligation as a result of a past event; it is probable that an outflow of resources will be required to settle the obligation; and the amount can be reliably estimated.

Provisions relate to make-good obligations arising from leases of office space. The non-current portion will be utilised by 2034.

	($000s)
Balance at 1 April 2015	854
Provisions made during the year	126
Provisions utilised during the year	(18)
Unwinding of discount	30
Foreign exchange adjustment	43
Balance at 31 March 2016	**1,035**
Current	63
Non-current	972

14. SHARE CAPITAL

At 31 March	Note	2016 (000s)	2015 (000s)
Balance at 1 April		136,008	127,610
Issue of ordinary shares – capital raise		–	7,359
Issue of ordinary shares – acquisition of Monchilla, Inc.		–	238
Issue of ordinary shares – Employee Restricted Share Plan	20	545	592
Issue of ordinary shares – exercising of employee options	20	155	71
Issue of ordinary shares – Director exercising options		33	67
Issue of ordinary shares – Directors fees and key management		4	22
Issue of ordinary shares – RSU schemes	20	69	49
Ordinary shares on issue at 31 March		**136,814**	**136,008**
Treasury shares		(791)	(735)
Ordinary shares on issue at 31 March excluding treasury shares		**136,023**	**135,273**

All shares have been issued, are fully paid and have no par value.

During the period, the Company issued 544,566 shares under the Employee Restricted Share Plan (RSP), at an average price of $17.13 (2015: 591,169, $21.48).

During the period, employees exercised 154,780 stock options under the US Equity Incentive Scheme, with an average exercise price of $4.37 (2015: 71,496, $5.37).

During the period, a Director exercised 33,334 share options under the US Equity Incentive Scheme in his capacity as an advisor, with an average exercise price of $4.97 (2015: 66,666, $4.97).

During the period, the Company issued 4,093 shares at a weighted average price of $17.10 to Lee Hatton in lieu of cash payment for Directors' fees (2015: 2,173 shares were issued to Lee Hatton at $16.10 and 20,000 shares to a key member of management at a price of $16.81).

The Company issued 68,779 shares upon vesting of RSUs granted to employees under the US RSU scheme, the Australia RSU scheme and the New Zealand RSU scheme, with an average price of $18.41 (2015: 49,366, $18.27).

Treasury shares includes unvested RSP shares and unvested shares issued on the acquisition of Monchilla, Inc.

15. RECONCILIATION OF OPERATING CASH FLOWS

Year ended 31 March	**2016 ($000s)**	**2015 ($000s)**
Net loss after tax	(82,464)	(69,534)
Adjustments:		
Depreciation	6,426	4,697
Amortisation	22,717	13,293
Deferred tax	(1,228)	(1,132)
Tax losses utilised	846	(846)
Gain on foreign exchange transactions	(1,780)	(2,025)
Loss on disposal of property, plant and equipment	373	239
Employee share-based payments	14,737	9,172
Non-employee share-based payments	410	1,346
Bad debts	542	347
Other non-cash items	276	–
Changes in working capital:		
Increase in trade receivables and prepayments	(7,301)	(7,534)
Decrease in interest receivable	1,675	188
Increase in trade payables and accruals	5,652	6,032
Increase/(decrease) in current tax payable	(1,907)	1,471
Increase in employee entitlements	6,453	4,915
Increase/(decrease) in income in advance	(197)	748
Net cash flows from operating activities	**(34,770)**	**(38,623)**

16. RELATED PARTIES

The following transactions were carried out with related parties:

Loans to key management

Year ended 31 March	2016 ($000s)	2015 ($000s)
Opening balance	612	2,776
Loans repaid in the period	(617)	(2,261)
Interest charged on loans	5	97
Closing balance	**–**	**612**

Secured loans were issued to key management to purchase shares in the Company at market price. Simple interest is accrued at a rate of 4% per annum, with the loans and interest repayable three years from the date of issue. The fair value of the loans does not materially differ from the carrying value.

Key management personnel Key management personnel are defined as those persons having authority and responsibility for planning, directing and controlling the activities of the Group, directly or indirectly, and include the Directors, the Chief Executive, his direct reports and the country managers. The following table summarises remuneration paid to key management personnel.

Year ended 31 March	2016 ($000s)	2015 ($000s)
Short-term employee benefits	7,094	4,878
Directors' fees	796	515
Options (under the Employee Share Options Scheme)	201	139
Restricted stock units	2,146	998
Share-based payments (under the Employee Restricted Share Plan)	2,959	1,744

The table above excludes expenses of $485,000 paid to Directors in strategic advisory fees, outside their capacity as Directors (2015: $1,086,000).

A number of key management personnel, or their related parties, hold positions in other entities that result in them having control or significant influence over the financial or operating policies of these entities. A number of these entities subscribe to the Xero services provided by the Group. None of these related party transactions are significant to either party.

No amounts with any related parties have been written off or foregone during the year (2015: Nil).

17. FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT OBJECTIVES

Financial instruments Financial instruments recognised in the Statement of Financial Position include cash and cash equivalents and short-term deposits, receivables and payables and derivative financial instruments. The Group's policy is that no trading in financial instruments shall be undertaken.

The Group assesses at each reporting date whether there is objective evidence that a financial asset or a group of financial assets is impaired. Financial assets are impaired when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the receivables. The carrying amount of an asset is reduced through the use of a provision account, and the amount of the loss is recognised in the Income Statement. When a receivable is uncollectible, it is written off against the provision account for receivables. Subsequent recoveries of amounts previously written off are credited against the Income Statement.

Capital management The capital structure of the Group consists of equity raised by the issue of ordinary shares in the Parent. The Group manages its capital to ensure that entities in the Group are able to continue as going concerns. The Group is not subject to any externally imposed capital requirements.

Classification and fair values Xero has carried out a fair value assessment of its financial assets and liabilities at 31 March 2016 in accordance with NZ IFRS 13 Fair Value Measurement.

The Group's hedging derivatives are recognised at fair value. Fair values are calculated using forward exchange rates that are quoted in an active market (level 2 on the fair value hierarchy).

The carrying value of the Group's other financial instruments do not materially differ from their fair value.

	Loans and receivables ($000s)	Hedging instruments at fair value ($000s)	Financial liabilities at amortised cost ($000s)	Total carrying value ($000s)
At 31 March 2016				
Assets				
Cash and cash equivalents	39,024	–	–	39,024
Term deposits	145,000	–	–	145,000
Trade and other receivables	20,635	–	–	20,635
Short-term derivative assets	–	358	–	358
Total financial assets	**204,659**	**358**	**–**	**205,017**
Liabilities				
Trade and other payables	–	–	18,805	18,805
Short-term derivative liabilities	–	3,983	–	3,983
Total financial liabilities	**–**	**3,983**	**18,805**	**22,788**
At 31 March 2015				
Assets				
Cash and cash equivalents	58,866	–	–	58,866
Term deposits	210,000	–	–	210,000
Trade and other receivables	16,847	–	–	16,847
Short-term derivative assets	–	3,151	–	3,151
Loans to key management	612	–	–	612
Total financial assets	**286,325**	**3,151**	**–**	**289,476**
Liabilities				
Trade and other payables	–	–	12,227	12,227
Short-term derivative liabilities	–	130	–	130
Total financial liabilities	**–**	**130**	**12,227**	**12,357**

The main risks arising from the Group's financial instruments are interest rate risk, liquidity risk, credit risk and foreign currency risk.

Interest rate risk The Group's interest rate risk arises from its cash and cash equivalents, and short-term deposit balances. Cash and cash equivalents comprise cash on hand, deposits held at call with banks, other short-term and highly liquid investments with original maturities of 90 days or less. Balances are placed on short-term deposit at fixed rates. The repricing of these exposes the Group to cash flow interest rate risk. The Group does not enter into interest rate hedges.

Management regularly reviews its banking arrangements to ensure that it achieves the best returns on its funds while maintaining access to the liquidity levels necessary to service the Group's day-to-day activities.

The interest rate repricing profiles of the Group's financial assets and liabilities subject to interest rate risk are:

	Carrying value ($000s)	3 months or less ($000s)	3-6 months ($000s)	6-12 months ($000s)
At 31 March 2016				
Financial assets				
Cash and cash equivalents	39,024	39,024	–	–
Short-term deposits	145,000	51,000	42,000	52,000
Total	**184,024**	**90,024**	**42,000**	**52,000**
At 31 March 2015				
Financial assets				
Cash and cash equivalents	58,866	58,866	–	–
Short-term deposits	210,000	41,000	71,000	98,000
Loans to key management	612	–	612	–
Total	**269,478**	**99,866**	**71,612**	**98,000**

At 31 March 2016, if interest rates had been 1.0% higher/lower with all other variables held constant, the impact on the interest income, net loss and accumulated losses of the Group would have been $1.84m lower/higher (2015: $2.25m). This analysis assumes that the cash and cash equivalents and short-term deposits balance was consistent with the year end balance throughout the year.

Liquidity risk Liquidity risk is the risk that the Group cannot pay contractual liabilities as they fall due. At 31 March 2016 the Group held cash and cash equivalents of $39.0 million and term deposits of $145.0 million. The Group has sufficient liquidity to meet its cash flow requirements for the foreseeable future. The Group has no debt.

The undiscounted contractual cash flows of the Group's non-derivative financial liabilities are equal to the carrying value and are due within 12 months or less. The Group's exposure to undiscounted gross cash flows from derivative financial liabilities are:

	Carrying amount ($000s)	Contractual cash flows ($000s)	0-6 months ($000s)	6-12 months ($000s)
At 31 March 2016				
Forward exchange contracts	3,983	–	–	–
Inflows	–	84,634	40,765	43,869
Outflows	–	(89,175)	(43,139)	(46,036)
	3,983	**(4,541)**	**(2,374)**	**(2,167)**
At 31 March 2015				
Forward exchange contracts	130	–	–	–
Inflows	–	10,357	1,865	8,492
Outflows	–	(10,705)	(1,887)	(8,818)
	130	**(348)**	**(22)**	**(326)**

Credit risk Where the Group has a receivable from another party, there is a credit risk in the event of non-performance by that other party. Financial instruments that potentially subject the Group to credit risk principally consist of cash and cash equivalents, short-term deposits, derivatives and receivables.

The Group manages credit risk by placing its cash and short-term deposits with high credit quality financial institutions. The credit risk associated with trade receivables is small because of the inherently low individual transaction value and the spread over many customers.

Maximum exposure to credit risk at balance date

At 31 March	2016 ($000s)	2015 ($000s)
Cash and cash equivalents	39,024	58,866
Short-term deposits	145,000	210,000
Trade and other receivables	20,635	15,747
Derivative financial assets	358	3,151
Non-current receivables	2,004	1,712
Total	**207,021**	**289,476**

Foreign currency risk The Group faces the risk of movements in foreign currency exchange rates in relation to the New Zealand dollar. The Group has material operations in three other currencies, being Great British pounds (GBP), Australian dollars (AUD) and United States dollars (USD). As a result the Group's Income Statement and Statement of Financial Position can be affected by movements in exchange rates.

The Group's exposure to monetary foreign currency financial instruments is outlined below in New Zealand dollars:

	AUD ($000s)	USD ($000s)	GBP ($000s)
At 31 March 2016			
Exposures			
Cash and cash equivalents	4,970	12,730	4,512
Trade and other receivables	8,436	1,310	3,308
Trade and other payables	(2,726)	(3,034)	(2,443)
Derivative financial instruments	(42,925)	60,885	–
Total foreign currency exposure from financial instruments	**(32,245)**	**71,891**	**5,377**
At 31 March 2015			
Exposures			
Cash and cash equivalents	3,039	28,229	1,477
Trade and other receivables	5,262	2,480	2,747
Trade and other payables	(3,058)	(4,005)	(2,771)
Derivative financial instruments	(16,152)	33,751	–
Total foreign currency exposure from financial instruments	**(10,909)**	**60,455**	**1,453**

Xero is exposed to currency risk from the operations of foreign subsidiaries and foreign currency denominated expenses in the Parent company. The significant exposure is United States dollar outflows and Australian dollar inflows. The Group's treasury policy requires a portion of the next 12 months cash flows to be hedged with forward exchange contracts, to reduce the impacts of short-term movements in the exchange rate.

As at 31 March, a movement of 10% in the New Zealand dollar would impact the Income Statement and Statement of Changes in Equity (after hedging) as detailed in the table below:

	10% decrease		10% increase	
	2016 ($000s)	2015 ($000s)	2016 ($000s)	2015 ($000s)
Impact on:				
Net earnings before income tax	(1,894)	6,042	1,550	(4,934)
Equity (before income tax)	1,899	9,512	(1,554)	(7,773)

This analysis assumes a movement in the New Zealand dollar across all currencies and only includes the effect of foreign exchange movements on monetary financial instruments. All other variables remain constant.

18. HEDGE ACCOUNTING

The Group uses derivatives in the form of forward exchange contracts (FECs) to reduce the risk that movements in the exchange rate will affect the Group's New Zealand dollar cash flows. These hedges have been designated as a hedge of a highly probable forecast transaction (a cash flow hedge under NZ IAS 39: Financial instruments recognition and measurement). The Group's policy is to hedge a portion of the next 12 months forecasted cash flows.

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised in other comprehensive income. The gain or loss relating to the ineffective portion is recognised immediately in the Income Statement. Amounts accumulated in equity are reclassified to the Income Statement in the periods when the hedged transaction affects profit and loss.

During the period, a hedging loss of $643,000 (before taxation) was recognised in other comprehensive income (2015: gain of $5,057,000). During the year, a gain of $6,003,000 (before taxation) was reclassified out of other comprehensive income to the Income Statement (2015: gain of $2,036,000). The remaining balance will be reclassified to the Income Statement in the 12 months following 31 March 2016.

Hedge position

At 31 March	2016 Fair value ($000s)	2016 Notional amount hedged (NZ$000s)	2015 Fair value ($000s)	2015 Notional amount hedged (NZ$000s)
Short-term derivative assets				
Buy USD – Sell NZD	207	6,315	2,348	35,715
Buy NZD – Sell AUD	151	12,341	803	15,486
Total	**358**		**3,151**	
Short-term derivative liabilities				
Buy USD – Sell NZD	(3,421)	58,420	(126)	9,346
Buy NZD – Sell AUD	(562)	30,241	(4)	1,021
Total	**(3,983)**		**(130)**	

19. CONTINGENCIES

There were no contingent liabilities at 31 March 2016 (2015: Nil).

20. SHARE-BASED PAYMENTS

The Group operates equity-settled, share-based compensation plans, under which employees provide services in exchange for non-transferable options, Restricted Stock Units (RSUs) or shares. The value of the employee services rendered for the grant of non-transferable options, RSUs and shares is recognised as an expense over the vesting period, and the amount is determined by reference to the fair value of the options, RSUs and shares granted.

Employee Restricted Share Plan

The Xero Limited Employee Restricted Share Plan (RSP) was introduced for employees and executives of the Group. Under the RSP, ordinary shares in Xero Limited are issued to a trustee, Xero Trustee Limited, a wholly owned subsidiary, and allocated to participants, on grant date, using funds lent to them by the Company.

The shares are beneficially owned by the participants. The length of the retention period before the shares vest is between one and three years. If the individual is still employed by the Group at the end of this specific period, the employee is given a bonus that must be used to repay the loan, and shares are then transferred to the employee. The weighted average grant date fair value of restricted shares issued during the year was $17.44 (2015: $21.32) and was determined by the share price on grant date. Shares with a grant date fair value of $9,189,000 vested during the year (2015: $5,825,000). The Group has no legal or constructive obligation to repurchase the shares or settle the RSP for cash.

	2016 Number of shares (000s)	2015 Number of shares (000s)
Unvested shares as at 1 April	607	377
Granted	615	644
Forfeited	(126)	(52)
Vested	(488)	(362)
Unvested shares at 31 March – allocated to employees	**608**	**607**
Forfeited shares not yet reallocated – held by Trustee	65	9
Total	**673**	**616**
Ageing of unvested shares		
Balance of shares to vest within one year	274	267
Balance of shares to vest after one year	334	340
Total unvested shares at 31 March	**608**	**607**

The number of shares awarded pursuant to the RSP does not equal the number of shares created for the scheme, as forfeited shares are held in the trust and reissued.

Share Options Scheme

Options are granted to selected employees, Directors and service providers. The exercise price of the granted options is equal to the market price of the shares on the grant date.

Options are conditional on the completion of the necessary years' service (the vesting period). The options' tranches are exercisable over one to five years from the grant date. No options can be exercised later than the second anniversary of the final vesting date (a total of four to six years from the grant date). There were 58 holders of options at 31 March 2016 (2015: 70).

The Group has no legal or constructive obligation to repurchase or settle the options in cash.

Movements in the number of options outstanding and their related weighted average exercise prices are as follows:

	2016 Weighted average exercise price ($)	2016 Options (000s)	2015 Weighted average exercise price ($)	2015 Options (000s)
Outstanding at 1 April	16.52	901	18.57	936
Granted	18.07	367	16.22	323
Forfeited	16.50	(259)	32.30	(207)
Exercised	3.73	(188)	5.32	(138)
Expired	–	–	22.99	(13)
Outstanding at 31 March	**20.18**	**821**	**16.52**	**901**
Exercisable at 31 March	21.60	305	16.71	193

Options outstanding at the end of the year have the following expiry dates and exercise prices:

Granted	Expiry date	Exercise price ($)	2016 Options (000s)	2015 Options (000s)
2012-13	2017-18	2.75	25	120
2012-13	2016-17	3.82	–	47
2012-13	2016-17	5.31	80	94
2012-13	2016-17	4.97	–	33
2012-13	2016-17	7.70	4	4
2013-14	2017-18	17.40	82	98
2013-14	2017-18	32.17	40	42
2013-14	2017-18	38.24	140	140
2014-15	2018-19	16.81	–	40
2014-15	2018-19	16.14	58	58
2014-15	2019-20	16.05	–	200
2014-15	2019-20	16.85	25	25
2015-16	2019-20	19.51	176	–
2015-16	2019-20	17.14	125	–
2015-16	2019-20	16.00	66	–
			821	**901**

The weighted average fair value of options granted during the year, determined using the Black-Scholes valuation model, was $5.45 per option (2015: $7.14).

The significant inputs into the model were the market share price at grant date, the exercise price shown above, the expected annualised volatility of between 43% and 44%, a dividend yield of 0%, an expected option life of between one and six years and an annual risk-free interest rate of between 2.6% and 2.7%.

The volatility measured is the standard deviation of continuously compounded share returns and is based on a statistical analysis of daily share prices in the past one to six years.

Restricted Stock Units

No cash consideration is required to be paid to exercise the RSUs. The fair value of RSUs granted in the year ended 31 March 2016 was $7,166,000 (2015: $10,938,000) as determined by the market value of the shares on grant date. The RSUs are conditional on the employees completing up to three years' service (the vesting period) and are exercisable in equal amounts over the vesting period.

	2016 Weighted average exercise price ($)	2016 RSUs (000s)	2015 Weighted average exercise price ($)	2015 RSUs (000s)
Outstanding at 1 April	17.68	531	38.24	21
Granted	16.94	423	18.22	600
Forfeited	17.10	(175)	35.59	(33)
Converted to shares	18.06	(69)	19.26	(49)
Surrendered to pay payroll tax	24.09	(5)	27.65	(8)
Outstanding at 31 March	**17.30**	**705**	**17.68**	**531**

21. COMMITMENTS

Operating lease commitments

The Group leases offices and motor vehicles under non-cancellable operating lease agreements. The lease terms are between 1 and 12 years. A number of lease agreements are renewable at the end of the lease periods at a market rate.

The future minimum lease payments under non-cancellable operating leases are as follows:

At 31 March	2016 ($000s)	2015 ($000s)
Within one year	8,112	6,791
After one year but not more than five years	31,588	24,506
More than five years	23,323	22,490
	63,023	**53,787**

Xero leases two properties that have been sublet due to being surplus to requirements. The lease and sublease are on equivalent terms.

The total future minimum sublease payments expected to be received under non-cancellable subleases for office space at 31 March 2016 is $1,920,000 (2015: $530,000).

Capital commitments

Capital commitments of $3,950,000 for building fitouts were contracted for at 31 March but not yet incurred (2015: $1,496,000).

22. GROUP ENTITIES

Consolidation subsidiaries are all entities over which the Group has control. The Group controls an entity when the Group is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are deconsolidated from the date that control ceases.

Intercompany transactions and balances between Group companies are eliminated on consolidation.

The financial statements of each of the Group's subsidiaries are prepared in the functional currency of that entity. The functional currency is determined for each entity based on factors such as the principal trading currency. The assets and liabilities of these entities are translated at exchange rates existing at balance date. Revenue and expenses are translated at rates approximating the exchange rates ruling at the dates of the transactions. The exchange gains or losses arising on translation are recorded in other comprehensive income and accumulated in the foreign currency translation reserve in equity.

	Principal activity	Country of incorporation	Balance date	Interest 2016 (%)	Interest 2015 (%)
Xero (NZ) Limited	Limited risk reseller	New Zealand	31 March	100	100
Xero (UK) Limited	Limited risk reseller	United Kingdom	31 March	100	100
Xero Australia Pty Limited	Limited risk reseller	Australia	31 March	100	100
Xero, Inc.	Limited risk reseller	United States	31 March	100	100
Xero (Singapore) Pte. Ltd*	Service provider	Singapore	31 December	100	-
Monchilla, Inc.	Payroll software	United States	31 December	100	100
Xero Trustee Limited	Trustee	New Zealand	31 March	100	100

* Incorporated in March 2016

23. EVENTS AFTER THE BALANCE SHEET DATE

There were no significant events between balance date and the date these financial statements were authorised for issue.

Directors' Responsibilities Statement

The Directors are required to prepare financial statements for each financial year that present fairly the financial position of the Group and its operations and cash flows for that period.

The Directors consider these financial statements have been prepared using accounting policies suitable to the Group's circumstances, which have been consistently applied and supported by reasonable judgements and estimates, and that all relevant financial reporting and accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements.

The Directors are responsible for keeping proper accounting records that disclose with reasonable accuracy, at any time, the financial position of the Group and to enable them to ensure that the financial statements comply with the Companies Act 1993. They are also responsible for safeguarding the assets of the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Board of Directors of the Company authorised these financial statements for issue on 12 May 2016.

For and on behalf of the Board of Directors

Chris Liddell
Chairman
Xero Limited
12 May 2016

Graham Smith
Director
Xero Limited
12 May 2016

Corporate Governance

The Board recognises the importance of good corporate governance, particularly its role in delivering improved corporate performance and protecting the interests of all stakeholders.

The Board is responsible for establishing and implementing the Company's corporate governance frameworks, and is committed to fulfilling this role in accordance with best practice while observing applicable laws and the NZX Corporate Governance Best Practice Code (NZX Code).

This section sets out the Company's commitment to good corporate governance and addresses the Company's compliance with the NZX Code, using the structure of the nine principles published in the Corporate Governance in New Zealand – Principles and Guidelines issued by the Financial Markets Authority (FMA Principles).

PRINCIPLE 1 – ETHICAL STANDARDS

Directors should set high standards of ethical behaviour, model this behaviour, and hold management accountable for delivering these standards throughout the organisation.

The Board maintains high standards of ethical conduct and the Chief Executive and broader management team are responsible for ensuring that high standards of ethical conduct are maintained by all staff. Employees are made aware of, and required to comply with, the Company's Code of Conduct.

The Code of Conduct is available in the Investors section of the Company's website, and covers the practices necessary to maintain confidence in the Company's integrity; the practices necessary to take into account the Company's legal obligations and reasonable expectations of its stakeholders; and the responsibility and accountability of individuals for reporting and investigating reports of unethical practices.

Conflicts of interest The Board Charter (available in the Investors section of the Company's website) outlines the Board's policy on conflicts of interest. Where conflicts of interest do exist, Directors do not exercise their right to vote in respect of such matters. An interests register is maintained to record any interests that have been disclosed by Directors.

The particulars of entries made in the interests register for the period 1 April 2015 to 31 March 2016 are set out in the Disclosures section of this Report.

PRINCIPLE 2 – BOARD COMPOSITION AND PERFORMANCE

To ensure an effective board, there should be a balance of independence, skills, knowledge, experience and perspectives.

The Board is the overall and final body responsible for all decision-making within the Company, having a core objective to effectively represent and promote the interests of shareholders with a view to adding long-term value to the Company.

The Board Charter describes the Board's role and responsibilities and regulates internal Board procedures; a copy of this document is available in the Investors section on the Company's website.

The Board has the responsibility to work to enhance the value of the Company in the interests of the Company and the shareholders.

The Board directs, and supervises the management of, the business and affairs of the Company including, in particular:

- ensuring that the Company's goals are clearly established, and that strategies are in place for achieving them;
- ensuring that there is an ongoing review of performance against the Company's strategic objectives;
- approving transactions relating to acquisitions and divestments, and capital expenditure above delegated authority limits;
- ensuring that there is ongoing assessment of business risks and that there are appropriate control and accountability systems in place to manage them;
- establishing policies aimed at strengthening the performance of the Company, including ensuring that management proactively seeks to build the business through innovation, initiative, technology, new products and the development of its business capital;
- monitoring the performance of management;
- appointing the Chief Executive, setting the terms of employment and, where necessary, terminating their employment; and
- approving and monitoring the Company's financial and other reporting and ensuring the Company's financial statements represent a true and fair view.

Delegation To enhance efficiency, the Board has delegated some of its powers to Board Committees and other powers to the Chief Executive. The terms of the delegation by the Board to the Chief Executive are documented in the Board Charter and are set out in the Company's Delegated Authority Framework. This framework also establishes the authority levels for decision-making within the Company's management team.

Composition of the Board The Board is composed of experienced executives based in New Zealand, Australia, and the United States, with a broad and diverse range of technology, financial, sales, and general business experience. At 31 March 2016, the Board comprised eight Directors as follows:

- Chris Liddell (Non-executive Chair)
- Rod Drury (Executive Director)
- Craig Elliott (Non-executive Director)
- Lee Hatton (Non-executive Director)
- Sam Morgan (Non-executive Director)
- Graham Smith (Non-executive Director)
- Bill Veghte (Non-executive Director)
- Craig Winkler (Non-executive Director)

A short biography of each Director is available at www.xero.com/about/investors/leadership.

Graham Shaw retired as a Director at the 2015 Annual Meeting, in July 2015.

Selection and role of Chairman The Chairman of the Board is elected by the non-executive Directors. The Board supports the separation of the roles of Chairman of the Board and the Chief Executive.

The Chairman's role is to manage the Board effectively, to provide leadership to the Board, and to facilitate the Board's interface with the Chief Executive.

Chris Liddell, the current Chairman of the Board, was elected to that role upon his appointment to the Board in February 2014. The Board has determined that Chris Liddell is an Independent Director.

Director independence The Board Charter requires that a minimum of two Directors be independent.

The Board takes into account the guidance provided under the NZX Listing Rules in determining the independence of Directors.

The Board will review any determination it makes as to a Director's independence on becoming aware of any information that may have an impact on the independence of the Director. For this purpose, Directors are required to ensure that they immediately advise the Board of any relevant new or changed relationships to enable the Board to consider and determine the materiality of the relationships. The interests register is maintained to record these relationships.

As at 31 March 2016, the Board considers that Chris Liddell, Craig Elliott, Lee Hatton, Sam Morgan, Graham Smith and Bill Veghte are Independent Directors. The Board has determined that Rod Drury is not an Independent Director because of his executive responsibilities and substantial shareholding, and that Craig Winkler is not an Independent Director because of his substantial shareholding.

Nomination and appointment The procedures for the appointment and removal of Directors are ultimately governed by the Company's Constitution.

In accordance with NZX Listing Rules, the Company communicates through the ASX and NZX markets announcements platforms that it accepts nominations for Directors, with such nominations to be considered by shareholders at the Company's Annual Meeting.

Directors receive formal letters of appointment setting out the arrangements relating to their appointment.

Retirement and re-election The Board acknowledges and observes the relevant Director rotation/retirement rules under the Company's Constitution and the NZX Listing Rules, meaning that the prescribed number of Directors, at a minimum, retire at the Company's Annual Meeting. These individuals may offer themselves for re-election as Directors at the Annual Meeting, at which they retire by rotation.

Board access to information and advice Directors have the ability to access Group records and information required to fulfill their roles as Directors. All Directors have access to the senior management team, including the Company Secretary, to discuss issues or obtain information on specific areas in relation to items to be considered at Board meetings or other areas as they consider appropriate.

The Company Secretary is responsible for supporting the effectiveness of the Board by ensuring that policies and procedures are followed and coordinating the completion and dispatch of Board agendas and papers.

The Board, the Board Committees and each Director have the right, subject to the approval of the Chairman, to seek independent professional advice at the Company's expense to assist them to carry out their responsibilities. Further, the Board and Board Committees have the authority to secure the attendance at meetings of outsiders with relevant experience and expertise.

Director education All Directors are responsible for ensuring they remain current in understanding their duties as Directors.

Directors' share ownership Directors are encouraged to hold shares in the Company. All Directors and employees are required to comply with the Company's Securities Trading Policy and Guidelines in undertaking any trading in the Company's shares. A copy of this Policy can be found in the Investors section on the Company's website. The table of Directors' equity holdings in the Company is included in the Disclosures section of this Report.

Indemnities and insurance Deeds of Indemnity have been granted by the Company in favour of the Directors in relation to potential liabilities and costs they may incur for acts or omissions in their capacity as Directors.

The Directors' and Officers' liability insurance covers risks normally covered by such policies arising out of acts or omissions of Directors and employees in their capacity as such.

Board meetings The Board met for eight scheduled meetings during the financial year, where key financial and operational matters were considered as well as matters of strategic importance. The Board also approves certain matters by way of circular resolution, such as issues relating to equity under the Company's long term incentive schemes.

Executives regularly attend Board meetings and are also available to be contacted by Directors between meetings.

There were also separate meetings of the Board Committees during the year as necessary. Directors who are not members of the Committees may attend the Committee meetings.

Board Performance The Board has a formal review of its performance and areas of focus on an annual basis.

Feedback on relevant Board performance factors is provided by executive members to enhance the working relationship between the Board and management.

PRINCIPLE 3 – BOARD COMMITTEES

The Board should use committees where this will enhance its effectiveness in key areas, while still retaining board responsibility.

Board Committees The Board operates three Committees: the Audit and Risk Management Committee, the People and Remuneration Committee, and the Nominations Committee. The Charter of each Committee is in the Investors section on the Company's website.

The membership of each Committee at 31 March 2016 was:

- Audit and Risk Management Committee: Graham Smith (Chair), Chris Liddell, Craig Winkler, Lee Hatton
- People and Remuneration Committee: Sam Morgan (Chair), Chris Liddell, Craig Elliott, Bill Veghte, Lee Hatton
- Nominations Committee: Chris Liddell (Chair), Sam Morgan, Craig Winkler

Audit and Risk Management Committee Please see Principle 4 below for further details on the Audit and Risk Management Committee.

People and Remuneration Committee Please see Principle 5 below for further details on the People and Remuneration Committee.

Nominations Committees The Board has established a Nominations Committee whose role is to identify and recommend to the Board individuals for nomination as members of the Board and its Committees, taking into account such factors as it deems appropriate, including experience, qualifications, judgement and the ability to work with other Directors.

PRINCIPLE 4 – REPORTING AND DISCLOSURE

The board should demand integrity in financial reporting and in the timeliness and balance of corporate disclosures.

The Board is committed to a transparent system for auditing and reporting of the Company's financial performance. The Board has established an Audit and Risk Management Committee, which performs a central role in achieving this goal. The Audit and Risk Management Committee has at least two members who are financial experts that possess accounting and audit skills.

The Audit and Risk Management Committee's principal functions are:

- to assist the Board in ensuring that appropriate accounting policies and internal controls are established and followed;
- to assist the Board in producing accurate financial statements in compliance with all applicable legal requirements and accounting standards; and
- to ensure the efficient and effective management of business risks.

The Audit and Risk Management Committee has adopted a formal charter, a copy of which is available in the Investors section on the Company's website.

Corporate disclosures A copy of the Company's Market Disclosure and Communications Policy is available in the Investors section on the Company's website.

The Company complies with its continuous disclosure obligations under the NZX Listing Rules, the Financial Markets Conduct Act 2013, and the ASX Listing Rules.

PRINCIPLE 5 – REMUNERATION

The remuneration of directors and executives should be transparent, fair and reasonable.

The Board has a People and Remuneration Committee whose principal function is to oversee the Company's strategies and policies relating to organisational structure, culture, employee performance and development, succession planning, growth, and remuneration.

Performance management Formal procedures are in place to evaluate the performance of all of the Company's employees. This process is managed by the Head of HR/People (now the Chief People Officer) in liaison with the Chief Executive and the Chief Executive's direct reports as appropriate. This process was completed during the financial year.

Evaluations of the Chief Executive and the senior management team are based on a more involved set of criteria, including the performance of the business, the accomplishment of long-term strategic objectives and other non-quantitative objectives. During the financial year, performance evaluations of the Chief Executive and senior management team were completed as planned.

The People and Remuneration Committee has responsibilities that include reviewing and evaluating the performance of the Chief Executive against key performance objectives, reviewing the performance objectives for the Chief Executive for the following year, and monitoring the performance of each of the Chief Executive's direct reports.

Employee Incentives A key component of the Company's remuneration framework is the Company's long term incentive schemes, which are generally available to all employees. These schemes allow employees to be granted shares in the Company, which aligns the interests of those employees with the interests of shareholders and rewards participating employees for the creation of shareholder wealth.

Senior management participate in a short term incentive program, with remuneration under this program determined by the achievement of key performance indicators that are individually set for the participants in the program.

Director remuneration Directors' fees are currently set at a maximum of $850,000 for the non-executive Directors. The actual amount of fees paid to the Directors (whether in cash, shares, or options) in the financial year is set out in the Disclosures section of this Report, along with further detail on remuneration paid to Directors. The Company distinguishes the structure of non-executive Directors' remuneration from that of its Executive Director.

The People and Remuneration Committee is governed by a formal charter, a copy of which is available in the Investors section on the Company's website.

PRINCIPLE 6 – RISK MANAGEMENT

Directors should have a sound understanding of the key risks faced by the business. The board should regularly verify that the entity has appropriate processes that identify and manage potential and relevant risks.

As noted in Principle 4, one of the principal functions of the Audit and Risk Management Committee is to ensure the efficient and effective management of business risks.

The Company's senior management maintain a Risk Register which is reviewed at Audit and Risk Management Committee meetings, with certain aspects escalated to the Board as appropriate by the Audit and Risk Management Committee. Detailed reviews of certain risks appearing on the Risk Register are undertaken at Audit and Risk Management Committee meetings, as appropriate.

PRINCIPLE 7 – AUDITORS

The board should ensure the quality and independence of the external audit process.

Another purpose of the Audit and Risk Management Committee is to ensure the quality and independence of the audit process. The Chairman of the Audit and Risk Management Committee and the Chief Financial Officer work with the external auditors to plan the audit approach. All aspects of the audit are reported back to the Audit and Risk Management Committee and the auditors are given the opportunity at Audit and Risk Management Committee meetings to meet with the Committee, including without the Company's management being present.

The external auditors are responsible for planning and carrying out each audit and review, in accordance with applicable auditing and review standards. The Board ensures the auditor is remunerated fairly for the agreed scope of the statutory audit and audit-related services.

Non-audit work During the financial year, the external auditors did specific non-audit work, with approval from the Audit and Risk Management Committee. There was no compromise to the independence and objectivity of the audit process.

Please see Principle 4 above for further detail in relation to financial reporting and the role of the Audit and Risk Management Committee.

PRINCIPLE 8 – SHAREHOLDER RELATIONS

The board should foster constructive relationships with shareholders that encourage them to engage with the entity.

During the time that the Company has been listed on the NZX and the ASX, it has built a reputation of openness and has encouraged a high level of communication with shareholders and the market generally. It does this through numerous forms of communication including formal communication, social media, blogs, press releases and roadshows.

The Board encourages active participation by shareholders at the Annual Meeting of the Company, and allows shareholders to submit questions to the Board prior to or at the Annual Meeting, to be answered by the Board at the Annual Meeting.

The Board also facilitates questions to the external auditors during the Annual Meeting.

The Company maintains an up-to-date website providing a description of the business and links to key corporate governance documents.

PRINCIPLE 9 – STAKEHOLDER INTERESTS

The board should respect the interests of stakeholders taking into account the entity's ownership type and its fundamental purpose.

The Company has a wide range of stakeholders and aims to manage its business in a way which builds sustainable value and produces positive outcomes for stakeholders.

Community The Company is involved in sponsorship and volunteering in the wider community.

The Company has collaborated with BizDojo Wellington, whereby the Company provides mentorship and guidance to support business growth to a number of Wellington-based startups. The Company's mentors come from a wide range of backgrounds, with knowledge and experience in building scalable products, overseas markets, product roadmaps, team building, and more.

The Company is also very active volunteering in the community, with employees giving their time to worthy causes such as Enspiral Dev Academy, JHack, Code Camp Wellington, Software Engineering Students Association, Futureintech and ICT-Connect.

The Company has its own graduate and intern programs that support junior talent entering the technology industry. These programs are in place to develop the Company's own internal talent but also reflect the Company's commitment to the community by addressing youth unemployment and helping to develop the technology industry in New Zealand.

Diversity The Company recognises the importance of diversity in the workplace and its positive impact on the work environment and culture. The Board has approved measurable objectives for achieving diversity in the workplace. These are set out below, along with the Company's progress towards achieving them.

A copy of the Company's Diversity Policy is also available in the Investors section on the Company's website.

Objective A: Ensure that all recruitment campaigns generate a diverse pool of talent and that all hiring decisions are based on merit, taking into account the relevant skills, qualifications, and experience of all applicants and recognising the importance of diversity in the workforce.

Progress: The Company carries out the bulk of its recruiting efforts using its internal recruiting function. A diverse range of recruitment tools, job boards, social media channels and sourcing methods are used with the aim of maximisng the reach and breadth of talent sourcing and therefore maximising the diversity of the recruitment pool from which employees are selected. Selection processes are rigorous, involving appropriate screening, interviewing, competency based testing and reference checking to ensure all hiring decisions are made on merit, taking into account relevant hiring considerations. The importance of diversity is emphasised, and well understood by hiring managers and the internal recruitment team, both through recruitment-related training and communication of the Company's core values. A number of the Company's recruitment campaigns are aimed at increasing diversity in the workplace, such as sponsorship of and attendance at events like Women in Tech events, Rail Girls, Girl Code, SheSharp, graduate recruitment campaigns, the Company's graduate and intern programs, and publishing case studies that represent the Company's diverse workforce. The Company is particularly focused on programs to promote women in technology.

Objective B: Ensure that appropriate internal policies supporting and promoting diversity have been adopted and are well communicated to all employees.

Progress: The Company has adopted and communicated a Diversity Policy and a Code of Conduct, both of which support diversity in the workplace. Copies of the Company's Diversity Policy and Code of Conduct are made available to all staff on the Company's intranet, and are also available in the Investors section of the Company's website. The Company has recently reviewed, updated and communicated favourable parental leave and flexi-leave arrangements.

Objective C: Ensure that no impediments exist that restrict the ability to maintain a diverse workforce.

Progress: The Company's HR function actively ensures that there are no impediments that restrict the Company from maintaining a diverse workforce. The Company provides management training to its current and potential leaders, which includes training on being a successful leader and fostering a healthy and inclusive work environment. The Company provides numerous forums to its employees (including anonymous employee surveys) to enable and encourage its employees to raise any concerns that they may have in relation to their work environment.

Objective D: Continually review and monitor parity of working conditions and pay across the workforce.

Progress: The Company continually reviews the working conditions of all of its employees and reviews remuneration to ensure that it is merit-based and adequately reflects the responsibilities of the position. The Company conducts annual performance and salary reviews which provide visibility to management in relation to parity of working conditions and pay across its workforce. There are numerous ways in which employees can raise concerns about working conditions within the Company, and these are regularly communicated to staff.

Objective E: Reinforce internally and externally that Xero is an equal opportunity employer that does not discriminate on any of the prohibited grounds of discrimination, including gender, family status, sexual orientation, religious, ethical or political beliefs, ethnicity, disability, and age.

Progress: The composition of the Company's workforce demonstrates that it is an equal opportunity employer that does not discriminate on any of the prohibited grounds of discrimination. As discussed above, the Company takes active steps to monitor and encourage diversity in the workforce.

Gender Diversity Two senior executive roles have recently been filled by females. Kirsty Godfrey-Billy, the Company's new Chief Accounting Officer, and Rachael Powell, the Company's new Chief People Officer both report to Sankar Narayan, the Company's Chief Financial Officer. Anna Curzon was also appointed to the role of Managing Director for New Zealand in February 2016 and plays a key role as one of the Company's regional leaders.

The proportion of females employed by the Company (and its wholly-owned subsidiaries) was as follows:

At 31 March	2016 Women	2016 Men	2016 Total	2016 %	2015 Women	2015 Men	2015 Total	2015 %
Directors	1	7	8	13%	1	8	9	11%
Officers*	0	6	6	0%	0	5	5	0%
Senior Executives**	2	10	12	17%	1	8	9	11%
All employees***	538	915	1,454	37%	430	731	1,161	37%

These figures include permanent full-time, permanent part-time, and fixed-term employees, but not contractors

**Officer is defined as a person who is concerned or takes part in the management of the Company and reports directly to the Board or reports directly to a person who reports to the Board*

***Senior Executives is defined as C-level executives and Country Managers. These figures do not include Kirsty Godfrey-Billy, the Company's new Chief Accounting Officer who started on 11 April 2016*

****One employee not declared*

Disclosures

ENTRIES RECORDED IN THE INTERESTS REGISTER

The Company maintains an Interests Register in accordance with the Companies Act 1993 and the Financial Markets Conduct Act 2013. The following are particulars of entries made in the Interests Register for the period 1 April 2015 to 31 March 2016.

Directors' interests Directors disclosed interests, or cessations of interest, in the following entities pursuant to section 140 of the Companies Act 1993 during the year ended 31 March 2016.

Director/Entity	Relationship
Sam Morgan	
Vend Limited	Director
Wynyard Group Limited	Investor
Goodnest Limited	Investor
CloudCannon Limited	Investor
Willis Bond Capital Partners No.2 Limited	Investor, Advisor
Jasmine Investment Trust No.3	Trustee
Jasmine Investment Holdings No.5 Limited	Director
P F Holdings Limited	Ceased to be a Director
Tokaroa Farm Limited	Ceased to be a Director

Director/Entity	Relationship
Craig Winkler	
Balance Labs, Inc.	Investor
Chaser Technologies Limited	Investor
Lee Hatton	
NAB Ventures Pty Limited	Director
BNZ Investment Services Limited	Ceased to be a Director
Graham Smith	
BlackLine Inc.	Director
Citrix Systems, Inc.	Director
Good Technology, Inc.	Ceased to be a Director
Bill Veghte	
VMTurbo, Inc.	Advisor
YourPeople, Inc. (Zenefits)	Investor

Share dealings of Directors Directors disclosed the following acquisitions and disposals of relevant interests in Xero shares during the year ended 31 March 2016.

Shares	Date of acquisition/disposal	Consideration per share	Number of shares acquired/ (disposed)
Graham Shaw*	23 July 2015	$18.34	(784)
Graham Shaw*	24 July 2015	$18.27	(35,226)
Lee Hatton**	10 August 2015	$17.64	1,984
Graham Shaw*	18-24 September 2015	$14.20	(40,000)
Graham Shaw*	27 October 2015	$15.98	(2,500)
Graham Shaw*	30 October 2015	$15.85	(57,500)
Bill Veghte***	12 November 2015	$13.05	15,321
Givia Pty Limited (Craig Winkler)****	26 November 2015	$20.01	(1,000,000)
Jasmine Investment Holdings Limited (Sam Morgan)*****	26 November 2015	$20.01	(500,000)
Anna Margaret Clare Drury, Rodney Kenneth Drury and Scott Moran (Rod Drury)******	26 November 2015	$20.01	(1,000,000)
Craig Elliott*******	1 December 2015	$4.97	33,334
Lee Hatton**	10 February 2016	$16.59	2,109

** Graham Shaw resigned as a Director on 22 July 2015*
*** The shares were issued to Lee Hatton as remuneration for her role as Director*
**** The shares acquired by Bill Veghte are held in the form of securities purchased in the US through OTC Markets as "XROLF". The consideration per share is shown in USD, and is the average price for the shares purchased. The date the shares were purchased is shown in US, EST*
***** The number of shares disposed represents 5.41% of Craig Winkler's total holdings prior to the disposal and 0.73% of the total number of shares on issue at 26 November 2015*
****** The number of shares disposed represents 9.76% of Sam Morgan's total holdings prior to the disposal and 0.37% of the total number of shares on issue at 26 November 2015*
******* The number of shares disposed represents 4.60% of Rod Drury's total holdings prior to the disposal and 0.73% of the total number of shares on issue at 26 November 2015*
********The shares acquired by Craig Elliott on 1 December 2015 were issued upon exercise of an equivalent number of options. Each option had an exercise price of $4.97. These shares were subsequently transferred to Private Nominees Limited as custodian for the benefit of Craig Elliott on 2 December 2015. In April 2015, Craig Elliott also transferred 66,666 shares to Private Nominees Limited, to be held by Private Nominees Limited as custodian for the benefit of Craig Elliott*

Share options	Date of grant	Exercise price	Number of options granted
Chris Liddell*	12 February 2016	$16.00	36,912
Bill Veghte**	12 February 2016	$16.00	29,530

**The options were granted to Chris Liddell as remuneration for his role as Director*
***The options were granted to Bill Veghte as remuneration for his role as Director*

Holdings of shares and options by Directors

At 31 March	2016 Number of shares	2016 Number of options	2015 Number of shares	2015 Number of options
Rod Drury	20,719,779	–	21,719,779	–
Craig Elliott*	100,000	–	66,666	33,334
Sam Morgan	4,622,609	–	5,122,609	–
Graham Shaw**	1,160,000	–	1,336,010	–
Craig Winkler (two holdings)	17,475,990	–	18,475,990	–
Chris Liddell***	15,000	147,556	15,000	110,644
Bill Veghte****	41,321	118,045	26,000	88,515
Lee Hatton*****	6,266	–	2,173	–
Graham Smith	–	–	–	–

**The shares are held by Private Nominees Limited as custodian for the benefit of Craig Elliott*
***Graham Shaw resigned as a Director on 22 July 2015*
****63,042 of the options granted to Chris Liddell vested (meaning that they were capable of being exercised) on 12 February 2016 but have not been exercised as at 29 April 2016. The 15,000 shares are held by FNZ Custodians Limited on behalf of Chris Liddell*
***** 50,433 of the options granted to Bill Veghte vested (meaning that they were capable of being exercised) on 12 February 2016 but have not been exercised as at 29 April 2016. The 41,321 shares are held by National Financial Services LLC on behalf of Bean Brook Farm 2013 Annuity Trust (the Trust). Bill Veghte is the trustee of the Trust and his immediate family are the beneficiaries. 15,321 of the shares are held in the form of securities purchased in the US through the OTC Markets as "XROLF"*
****** Lee Hatton was issued shares in lieu of cash, as remuneration for her role as Director, to the a value of $70,000. In addition to the 6,266 shares held by Lee Hatton (as noted above), 200 shares are held by Lee Hatton's spouse*

Remuneration of Directors Details of the total remuneration of, and the value of other benefits received by, each Director of Xero during the financial years ended 31 March:

	2016 Fees ($000s)	2016 Remuneration ($000s)	2015 Fees ($000s)	2015 Remuneration ($000s)
Rod Drury*	–	761	–	567
Craig Elliott	40	–	40	–
Sam Morgan	40	–	40	–
Graham Shaw**	15	–	50	–
Craig Winkler	40	–	40	–
Chris Liddell***	202	–	145	–
Bill Veghte****	161	–	116	–
Lee Hatton*****	72	–	68	–
Graham Smith	226	–	16	–
Total	**796**	**761**	**515**	**567**

**Rod Drury is an Executive Director and receives remuneration from Xero in the form of a salary and short-term incentives. He does not participate in the Employee Restricted Share Plan or receive remuneration in his capacity as Director*

*** Graham Shaw was paid $40,000 for his role as Director and $10,000 for his role as Chair of the Audit and Risk Management Committee in 2015. Graham Shaw resigned as a Director on 22 July 2015*

**** The 2016 figure represents the accounting expense that has been recognised for the financial year ended 31 March 2016 in respect of the options granted to Chris Liddell in his capacity as Director. Due to the three year vesting of the options, the current year expense includes options granted in 2014, 2015 and 2016; (2015: expense includes options granted in 2014 and 2015). The actual value of the options granted to Chris Liddell in the financial year ended 31 March 2016, at the time of grant, was $220,000*

***** The 2016 figure represents the accounting expense that has been recognised for the financial year ended 31 March 2016 in respect of the options granted to Bill Veghte in his capacity as Director. Due to the three year vesting of the options, the current year expense includes options granted in 2014, 2015 and 2016; (2015: expense includes options granted in 2014 and 2015). The actual value of the options granted to Bill Veghte in the financial year ended 31 March 2016, at the time of grant, was $176,000*

****** Lee Hatton was issued $70,000 worth of shares in lieu of cash and $2,000 in cash, as remuneration for her role as Director*

Employee remuneration The following table shows the number of employees (including employees holding office as Directors of subsidiaries) whose remuneration and benefits for the year ended 31 March 2016 were within the specified bands above $100,000.

The remuneration figures include all monetary and share-based payments actually paid during the course of the year ended 31 March 2016. The numbers below include 248 New Zealand-based current and former employees and 387 overseas-based current and former employees. The deterioration of the NZD over the year had a significant impact on foreign currency translation. 11% of the remuneration below relates to non-cash bonuses paid in respect of the Group's Share Schemes.

The table below includes the remuneration of Rod Drury ($761,000). No Director of a subsidiary receives or retains any remuneration or other benefits from Xero for acting as such.

Remuneration including equity based compensation	2016 Number of employees
100,000 to 109,999	108
110,000 to 119,999	85
120,000 to 129,999	68
130,000 to 139,999	56
140,000 to 149,999	49
150,000 to 159,999	40
160,000 to 169,999	26
170,000 to 179,999	31
180,000 to 189,999	21
190,000 to 199,999	19
200,000 to 209,999	17
210,000 to 219,999	18
220,000 to 229,999	13
230,000 to 239,999	12
240,000 to 249,999	4
250,000 to 259,999	7
260,000 to 269,999	2
270,000 to 279,999	7
280,000 to 289,999	6
290,000 to 299,999	2
300,000 to 309,999	7
310,000 to 319,999	2
320,000 to 329,999	1
330,000 to 339,999	1

Remuneration including equity based compensation	2016 Number of employees
340,000 to 349,999	1
350,000 to 359,999	2
370,000 to 379,000	2
380,000 to 389,000	3
390,000 to 399,999	1
400,000 to 409,999	1
440,000 to 449,999	4
450,000 to 459,999	1
470,000 to 479,999	1
480,000 to 489,999	2
510,000 to 519,999	1
550,000 to 559,999	1
570,000 to 579,999	1
590,000 to 599,999	2
730,000 to 739,999	1
740,000 to 749,999	1
760,000 to 769,999	1
820,000 to 829,999	1
910,000 to 919,999	1
1,080,000 to 1,089,999	1
1,200,000 to 1,209,999	1
1,210,000 to 1,219,999	1
1,320,000 to 1,329,999	1
1,660,000 to 1,669,999	1

Analysis of shareholding at 29 April 2016

	Number of holders	Number of shares	% of issued capital
1 to 1,000	12,514	4,176,980	3.05
1,001 to 5,000	2,931	6,486,477	4.74
5,001 to 10,000	419	3,003,606	2.19
10,001 to 100,000	343	8,128,700	5.94
100,001 and over	48	115,150,010	84.08
Grand total	**16,255**	**136,945,773**	**100.00**

There were 70 shareholders on the Company's New Zealand register holding less than a "minimum holding" (defined in the NZX Listing Rules as 25 shares) on 29 April 2016. There were also 551 shareholders on the Company's Australian register holding less than a marketable parcel of shares (defined in the ASX Listing Rules as a parcel of not less than AU$500), based on the closing price of Xero's shares on the ASX on 29 April 2016, being AU$15.00.

Twenty largest shareholders at 29 April 2016

Shareholder rank and name	Holding	% of total shares on issue
1. New Zealand Central Securities Depository Limited	37,774,041	27.58
2. Anna Margaret Clare Drury and Rodney Kenneth Drury and Scott Moran (Rod Drury)	20,719,779	15.13
3. Givia Pty Limited (Craig Winkler)	17,454,545	12.75
4. AP Investments (Hk) Limited	6,643,636	4.85
5. Jasmine Investment Holdings Limited (Sam Morgan)	4,622,609	3.38
6. Valar Ventures LP (Peter Thiel)	4,135,870	3.02
7. VV Xero Holdings LLC (Peter Thiel)	4,062,068	2.97
8. Hamish Craig Edwards and Tineke Jane Edwards and Andrew Paul Finch	3,899,203	2.85
9. Credit Suisse Securities (Europe) Limited	1,652,893	1.21
10. Nicola Jane Wilson and David Jonathan Wilson	1,526,884	1.11
11. Graham John Shaw and Delwyn Joy Shaw	1,120,000	0.82
12. Nelson Nien Sheng Wang and Pei Chun Ko	1,087,588	0.79
13. JP Morgan Nominees Australia Limited	968,187	0.71
14. W5 Limited	717,330	0.52
15. National Nominees Limited	685,511	0.50
16. Xero Limited (Employee Restricted Share Plan)	671,955	0.49
17. Craig Michael Walker and Catherine Claire Walker	663,898	0.48
18. JBWERE (NZ) Nominees Limited	544,553	0.40
19. HSBC Custody Nominees (Australia) Limited	472,429	0.34
20. Fletcher Matthew Oakley Brown and Karen Gail Oakley Harress	464,000	0.34

Substantial product holders According to notices given under the Financial Markets Conduct Act 2013, the following persons were substantial product holders in Xero Limited at 31 March 2016:

Substantial product holder	Quoted voting products in the Company in which a relevant interest is held
1. Anna Margaret Clare Drury and Rodney Kenneth Drury and Scott Moran (Rod Drury)	20,719,779
2. Givia Pty Limited (Craig Winkler)	17,454,545
3. Matrix Capital Management Company, LLC; Matrix Capital Management Master Fund, LP and Matrix Capital Management Fund II, LP (Matrix Capital Management)*	13,197,103
4. Valar Ventures LP; Valar Global Principals Fund I LP; Valar Global Fund I LP and VV Xero Holdings LLC (Peter Thiel)	8,528,516

**On 30 November 2012, Matrix Capital Management Company, LLC and Matrix Capital Management Master Fund, LP filed a Substantial Security Holder Notice disclosing a total interest of 11,489,934 ordinary shares in Xero Limited. On 16 October 2013, Xero Limited issued a further 991,736 ordinary shares to parties named in the Substantial Security Holder Notice dated 30 November 2012. On 13 March 2015, Xero Limited issued a further 715,433 ordinary shares to Matrix Capital Management Master Fund, LP and Matrix Capital Management Fund II, LP*

The total number of issued voting shares in Xero Limited at 31 March 2016 was 136,814,293 and the total number of issued voting shares of Xero Limited at 29 April 2016 was 136,945,773. Where voting at a meeting of shareholders is by voice or a show of hands, every shareholder present in person, or by representative, has one vote, and on a poll, every shareholder present in person, or by representative, has one vote for each fully paid ordinary share in the Company. There is, at the date of this Report (12 May 2016), no on-market buy-back for Xero's shares.

Restricted Securities The following shares are restricted securities or securities subject to voluntary escrow.

119,245 shares in the Company that were issued in connection with the acquisiton of 100% of the shares in Monchilla, Inc. in November 2014 are restricted securities until 6 November 2016, subject to the continued employment of Jack Couch and Nanjuan Shi respectively, with the Group.

671,955 shares are held on a restricted basis in connection with Xero's Employee Restricted Share Plan as at 29 April 2016.

Options There were 58 individuals holding a total of 820,546 options at 31 March 2016 and at 29 April 2016.

Restricted Stock Units (RSUs) There were 256 individuals holding a total of 705,405 RSUs at 31 March 2016 and 248 individuals holding a total of 473,606 RSUs at 29 April 2016. RSUs are a conditional contractual right to be issued an equivalent number of ordinary shares in Xero.

Foreign Exempt Listing ASX approved a change in the Company's ASX admission category from an ASX Listing to an ASX Foreign Exempt Listing, effective from the commencement of trading on 21 March 2016.

The Company continues to have a full listing on the NZX Main Board, and the Company's shares are still listed on the ASX. The Company is primarily regulated by the NZX, complies with the NZX Listing Rules, and is exempt from complying with most of the ASX Listing Rules (based on the principle of substituted compliance).

Waivers During the 12 months to 31 March 2016, Xero was granted or relied on various waivers from the NZX and ASX Listing Rules to allow the Directors to be remunerated in the form of equity securities (including both shares and options). More information on these waivers is set out below, and in the announcement posted on both the NZX and ASX on 17 June 2015.

Waivers (NZX) In July 2014, NZX Regulation granted the Company (1) a waiver from NZX Listing Rule 3.5.1 to allow the Company, subject to certain conditions, to remunerate the Directors, in their capacities as Directors, either in part or in whole by way of an issue of options, which would, upon exercise of such options, result in the issue of shares in the Company; and (2) a waiver from NZX Listing Rule 6.2.2, subject to certain conditions, with the effect that the Company is not required to prepare an Appraisal Report to accompany a Notice of Meeting provided to shareholders in reliance on the waiver granted in (1) that contains a resolution for the issue of options to Directors as remuneration. The Company relied on these waivers during the financial year ended 31 March 2016.

Waivers (ASX) In June 2015, ASX granted the Company (1) a waiver from ASX Listing Rules 10.13.3 and 10.13.5, subject to certain conditions,to the extent necessary to permit the Company's 2015 Notice of Meeting to contain a resolution seeking approval for the issue of a maximum of NZ$70,000 worth of shares to Lee Hatton as remuneration for her role as Director, in lieu of cash; and (2) a waiver from ASX Listing Rule 10.13.3, subject to certain conditions, to the extent necessary to permit the Company's 2015 Notice of Meeting to contain a resolution seeking approval for the grant of a maximum of NZ$220,000 worth of options to Chris Liddell and a maximum of NZ$176,000 worth of options to Bill Veghte, in their roles as Directors, in each case, in lieu of cash.

In addition to the waivers listed above, Xero has also been granted waivers from the ASX which are standard for a New Zealand company listed on the ASX including confirmation that ASX will accept financial statements denominated in New Zealand dollars and prepared and audited in accordance with New Zealand Generally Accepted Accounting Principles and Auditing Standards.

Company subsidiaries The Company has seven wholly-owned subsidiaries, consisting of a wholly-owned operating subsidiary in each of the Company's four core markets (being Australia, New Zealand, the United Kingdom, and the United States); Monchilla, Inc. (acquired by the Company in November 2014); Xero (Singapore) Pte. Ltd. (incorporated on 24 March 2016); and a wholly-owned subsidiary that acts as trustee in relation to the Company's long-term incentive scheme available to employees.

Subsidiary Company Directors The following people held office as Directors of subsidiary companies at 31 March 2016:

Xero (UK) Limited – Rod Drury, Gary Turner
Xero Australia Pty Limited – Rod Drury, Trent Innes
Xero (NZ) Limited – Rod Drury, Anna Curzon
Xero, Inc. – Rod Drury
Xero Trustee Limited – Rod Drury
Monchilla, Inc. – Rod Drury
Xero (Singapore) Pte. Ltd. – Rod Drury, Andy Lark, Alex Campbell

Trent Innes replaced Chris Ridd as a Director of Xero Australia Pty Limited on 30 March 2016, and Anna Curzon replaced Victoria Crone as a Director of Xero (NZ) Limited on 21 March 2016.

Graham Shaw retired as a Director of Xero Trustee Limited on 22 July 2015.

Annual Meeting Xero's Annual Meeting of shareholders will be held on Wednesday 20 July 2016 at 11am (NZT). A Notice of Annual Meeting and Proxy Form will be circulated to shareholders in June 2016.

Corporate Directory

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COMPANY NUMBERS:

183 0488 NEW ZEALAND

160 661 183 AUSTRALIAN REGISTERED BODY NUMBER (ARBN)

WEB ADDRESS:

WWW.XERO.COM

DIRECTORS:

CHRIS LIDDELL
CHAIRMAN

ROD DRURY

CRAIG ELLIOTT

LEE HATTON

SAM MORGAN

GRAHAM SMITH

BILL VEGHTE

CRAIG WINKLER

LEADERSHIP TEAM:

ROD DRURY
(CHIEF EXECUTIVE, CO-FOUNDER)

SANKAR NARAYAN
(CHIEF FINANCIAL OFFICER)

DUNCAN RITCHIE
(CHIEF PLATFORM OFFICER)

ANDY LARK
(CHIEF MARKETING AND BUSINESS OFFICER)

TONY STEWART
(CHIEF DATA OFFICER)

RACHAEL POWELL
(CHIEF PEOPLE OFFICER)

KIRSTY GODFREY-BILLY
(CHIEF ACCOUNTING OFFICER)

RUSS FUJIOKA
(US PRESIDENT)

TRENT INNES
(MANAGING DIRECTOR, AUS)

ANNA CURZON
(MANAGING DIRECTOR, NZ)

GARY TURNER
(MANAGING DIRECTOR, UK)

ALEX CAMPBELL
(MANAGING DIRECTOR, SG)

COMPANY SECRETARY:
MATT VAUGHAN

AUDITOR:

EY

LEGAL ADVISOR:

BELL GULLY

STOCK EXCHANGES:

THE COMPANY'S ORDINARY SHARES ARE LISTED ON THE NZX MAIN BOARD AND THE ASX

SHARE REGISTRAR:

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ANNUAL MEETING:

DATE: 20 JULY 2016
TIME: 11AM (NEW ZEALAND TIME)

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