XERO LIMITED ANNUAL REPORT **2011**

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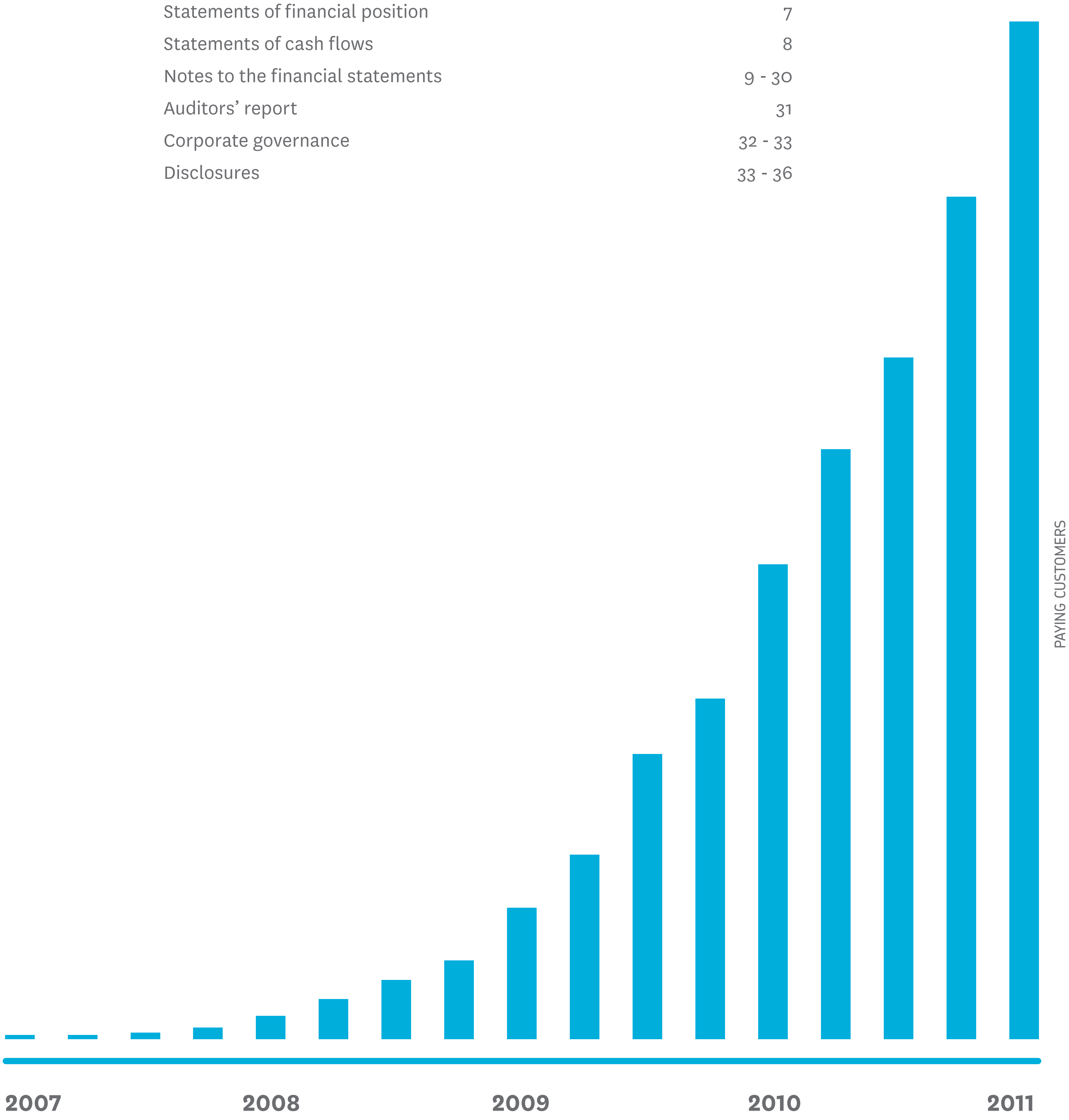

CHAIRMAN'S AND CHIEF EXECUTIVE'S REPORT

We are pleased to present our fourth Annual Report following another year of continued rapid growth and achievement of key milestones. Xero is now a global leader in the online accounting software sector and has established itself as the principal challenger to the incumbent market participants – Intuit, MYOB and Sage.

Revenue and Customer Growth

Operating revenue for the 2011 financial year was $9.3 million. This represents a tripling of revenue earned in the 2010 financial year – the second consecutive year the Company has tripled its revenues. At year-end, we had secured more than 36,000 paying customers from 100 countries. By comparison, we had 17,000 customers in 50 countries at the end of the previous year.

From February 2011, Xero has exceeded $1.0 million per month of revenue. The current annualised revenue run rate is, therefore, approximately $14.0 million. Revenue is expected to continue to grow strongly.

Since the business started, Xero has processed in excess of $35 billion of customer transactions. This is a strong endorsement of the quality and functionality of the software and the high level of acceptance of our online delivery model.

Xero has now established itself inside 2,200 accounting firms and continues to develop innovative features to gain broader adoption within the accounting community. A growing number of accounting practices are now 100% Xero. The accountant channel provides access to hundreds of thousands of small business customers.

Xero is renowned for its product innovation and the Company continues to change the face of the accounting software market as it combines small business and accountant processing into a single, cloud-based solution – all delivered at a much lower cost than our competitors.

The combination of product excellence, targeted marketing, best-in-class customer service and a global aspiration continues to underpin the Company's strong growth. With this platform, Xero is well positioned to achieve its goal of becoming an internationally successful New Zealand-based software company.

Markets

Xero's traction in its home market of New Zealand has been rapid. The Company now has a relationship with nearly every accounting firm in the country and through these firms is connected to thousands of small businesses. This success is being mirrored in Australia and the United Kingdom, giving us confidence that the approach is working.

In Australia, a Head Office has been established in Melbourne and a Managing Director appointed to take the business to the next level. In the United Kingdom, Xero is now regarded as an established brand. Both the Australian and United Kingdom operations continue to gain momentum and are well positioned to grow their share of the market.

Our sales operations in New Zealand, Australia and the United Kingdom are now all covering their direct costs.

Xero is increasing its activities in the US market. We are in the process of establishing an office in San Francisco, relocating some key staff from New Zealand and hiring locally in the US. The Company is building strategic partnerships and we have a number of marketing initiatives underway. The reception we have received so far has been extremely positive, which is a strong indicator that Xero can eventually capture a significant share of the vast US accounting software market.

Xero is leveraging its US Advisory Board, which includes Paypal founder and first outside Facebook investor, Peter Thiel. The Advisory Board's network has proved invaluable and allowed us to access market influencers and prospective strategic partners that we would not otherwise have been able to reach.

The US is important to the Company in the long-term; however, we will continue to take a measured approach to our entry into this market. This means carefully balancing investment in our existing business operations with the pursuit of growth opportunities, as we drive towards monthly break-even.

Product Development

Xero has continued to extend the capability of its core software (for example, payroll for small business and simple inventory) and continues to add new features. To date, we have delivered over 60 new releases of the software, which by software industry standards is exceptional.

We have furthered the integration of Xero with data-gathering service Yodlee, and have extended direct bank feeds to the United Kingdom, the US and many other markets.

In the 12 months since Xero Personal was launched, the feature set has advanced over six software releases and the product continues to attract new customers and favourable media reviews.

The Xero solution partner eco-system has continued to grow strongly and there are now over 40 publicly available online partner solutions that integrate seamlessly with the software. Many more are in the process of integration. This focus on connectivity will be an important element of Xero's US go-to-market strategy, as it will enable access to large numbers of users of complementary products.

An example of the effectiveness of this approach is our "Modern Practice" initiative, where working with Microsoft and a number of other software providers, Xero is core to an integrated suite of cloud-based solutions that allow accountants to run their entire practice without on-premise servers.

Financial Result

Operating revenue from customers was $9.3 million, while operating expenses totalled $18.0 million. The net loss after tax was $7.5 million. During the year, the Company reviewed the estimated useful life of its software and decided to increase this to a period of 3–5 years. The effect of this change was a decrease in amortisation costs for the year of $880,000.

CHAIRMAN'S AND CHIEF EXECUTIVE'S REPORT (CONTINUED)

The financial result is consistent with our expectations as we manage the investment in our existing business operations, while at the same time increasing our investment in the development of growth markets like the US. Ultimately these new markets will create significant shareholder value.

At year-end, Xero had cash reserves of $16.9 million.

The Year Ahead

Xero will continue its focus on product innovation backed by consistently excellent customer service. We will also continue to compete aggressively in our regional markets to further consolidate our leadership position, and we will increase the tempo of our US market activities as we develop our understanding of the market and refine our US version of the product.

Xero has a truly world-class team and we are extremely proud of their achievements to date. The Company will continue to invest in its people, as without them it would not be possible to achieve our ambitious goals.

We are excited about the Company's prospects for the next year and would like to thank all our shareholders for your ongoing support. We will continue to keep you informed as we achieve future milestones.

Phil Norman
Chairman

Rod Drury
Chief Executive

DIRECTORS' RESPONSIBILITIES STATEMENT

The Financial Reporting Act 1993 requires the Directors to prepare financial statements for each financial year that give a true and fair view of the financial position of the Company and Group and of the financial performance and cash flows for that period.

In preparing these financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent; and
- state whether applicable 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 Directors have pleasure in presenting the following financial statements for the year ended 31 March 2011.

The Board of Directors of the Company and Group authorised these financial statements for issue on 19 May 2011.

For and on behalf of the Board of Directors

Rod Drury
Director
19 May 2011

Graham Shaw
Director
19 May 2011

XERO LIMITED – INCOME STATEMENTS – FOR THE YEAR ENDED 31 MARCH 2011

	Notes	Group 2011 ($000s)	Group 2010 ($000s)	Parent 2011 ($000s)	Parent 2010 ($000s)
Operating revenue	*4*	9,341	3,158	8,858	3,868
Other income	*4*	325	237	325	237
Total operating revenue & other income		9,666	3,395	9,183	4,105
Operating expenses	*4*	18,017	12,874	17,655	13,543
Operating deficit		**(8,351)**	**(9,479)**	**(8,472)**	**(9,438)**
Net interest income	*4*	880	1,029	878	1,028
Net operating loss before tax		(7,471)	(8,450)	(7,594)	(8,410)
Share of profit of associate	*22*	10	–	–	–
Net loss before tax		(7,461)	(8,450)	(7,594)	(8,410)
Income tax expense	*5*	(26)	–	–	–
Net loss for the year attributable to the shareholders of the Company		**(7,487)**	**(8,450)**	**(7,594)**	**(8,410)**
Earnings per share					
Basic & diluted loss per share	*7*	($0.08)	($0.10)	($0.09)	($0.10)

The accompanying notes form an integral part of these financial statements

XERO LIMITED – STATEMENTS OF COMPREHENSIVE INCOME – FOR THE YEAR ENDED 31 MARCH 2011

	Group 2011 ($000s)	Group 2010 ($000s)	Parent 2011 ($000s)	Parent 2010 ($000s)
Net loss after tax	(7,487)	(8,450)	(7,594)	(8,410)
Other comprehensive income				
Exchange difference on translation of international subsidiaries	(53)	31	–	–
Other comprehensive (expense)/ income for the year, net of tax	(53)	31	–	–
Total comprehensive loss for the year attributable to the shareholders of the Company	**(7,540)**	**(8,419)**	**(7,594)**	**(8,410)**

The accompanying notes form an integral part of these financial statements

XERO LIMITED – GROUP – STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 31 MARCH 2011

	Notes	Share capital ($000s)	Treasury stock ($000s)	Share based payment reserve ($000s)	Accumulated losses ($000s)	Foreign currency translation reserve ($000s)	Total equity ($000s)
Group – Year ended 31 March 2011							
Restated balance at 1 April 2010		45,270	(738)	371	(20,560)	31	24,374
Net loss after tax		–	–	–	(7,487)	–	(7,487)
Currency translation movements		–	–	–	–	(53)	(53)
Total comprehensive income		**–**	**–**	**–**	**(7,487)**	**(53)**	**(7,540)**
Transactions with owners							
Issue of ordinary shares		4,040	–	–	–	–	4,040
Issue of ordinary shares for employee restricted share plan		858	(858)	–	–	–	–
Vesting of ordinary shares in employee restricted share plan		–	483	331	–	–	814
Balance as at 31 March 2011		**50,168**	**(1,113)**	**702**	**(28,047)**	**(22)**	**21,688**
Group – Year ended 31 March 2010							
Balance at 1 April 2009		17,130	–	–	(12,110)	–	5,020
Prior period restatement	23	–	(228)	190	–	–	(38)
Restated balance at 1 April 2009		17,130	(228)	190	(12,110)	–	4,982
Net loss after tax		–	–	–	(8,450)	–	(8,450)
Currency translation movements		–	–	–	–	31	31
Total comprehensive income		**–**	**–**	**–**	**(8,450)**	**31**	**(8,419)**
Transactions with owners							
Issue of ordinary shares		28,140	–	–	–	–	28,140
Share buy back		–	(740)	–	–	–	(740)
Vesting of ordinary shares in employee restricted share plan		–	230	181	–	–	411
Balance as at 31 March 2010 as restated		**45,270**	**(738)**	**371**	**(20,560)**	**31**	**24,374**

The accompanying notes form an integral part of these financial statements

XERO LIMITED – PARENT – STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 31 MARCH 2011

	Notes	Share capital ($000s)	Treasury stock ($000s)	Share based payment reserve ($000s)	Accumulated losses ($000s)	Total equity ($000s)
Parent – Year ended 31 March 2011						
Restated balance at 1 April 2010		45,270	(729)	371	(20,511)	24,401
Net loss after tax		–	–	–	(7,594)	(7,594)
Total comprehensive income		–	–	–	**(7,594)**	**(7,594)**
Transactions with owners						
Issue of ordinary shares		4,040	–	–	–	4,040
Issue of ordinary shares for employee restricted share plan		858	(858)	–	–	–
Vesting of ordinary shares in employee restricted share plan		–	474	331	–	805
Balance as at 31 March 2011		**50,168**	**(1,113)**	**702**	**(28,105)**	**21,652**
Parent – Year ended 31 March 2010						
Balance at 1 April 2009		17,130	–	–	(12,101)	5,029
Prior period restatement	23	–	(228)	190	–	(38)
Restated balance at 1 April 2009		17,130	(228)	190	(12,101)	4,991
Net loss after tax		–	–	–	(8,410)	(8,410)
Total comprehensive income		–	–	–	**(8,410)**	**(8,410)**
Transactions with owners						
Issue of ordinary shares		28,140	–	–	–	28,140
Share buy back		–	(740)	–	–	(740)
Vesting of ordinary shares in employee restricted share plan		–	239	181	–	420
Balance as at 31 March 2010 as restated		**45,270**	**(729)**	**371**	**(20,511)**	**24,401**

The accompanying notes form an integral part of these financial statements

XERO LIMITED – STATEMENTS OF FINANCIAL POSITION – AS AT 31 MARCH 2011

	Notes	Group 2011 ($000s)	Group 2010 Restated ($000s)	Group 2009 Restated ($000s)	Parent 2011 ($000s)	Parent 2010 Restated ($000s)	Parent 2009 Restated ($000s)
Assets							
Non-current assets							
Property, plant & equipment	8	466	367	375	384	333	364
Investment in subsidiaries	21	–	–	–	262	195	195
Investment in associate	22	207	–	–	200	–	–
Intangible assets	9	4,773	2,948	2,029	4,741	2,923	2,029
Trade & other receivables	11	441	411	398	423	411	398
Total non-current assets		**5,887**	**3,726**	**2,802**	**6,010**	**3,862**	**2,986**
Current assets							
Cash & cash equivalents	10	16,922	21,397	3,807	16,651	21,236	3,720
Deferred tax benefit	5	35	–	–	–	–	–
Trade & other receivables	11	1,503	958	280	1,187	780	239
Total current assets		**18,460**	**22,355**	**4,087**	**17,838**	**22,016**	**3,959**
Total assets		**24,347**	**26,081**	**6,889**	**23,848**	**25,878**	**6,945**
Liabilities							
Current liabilities							
Trade & other payables	12	2,659	1,707	1,887	2,196	1,477	1,934
Finance lease		–	–	6	–	–	6
Total current liabilities		**2,659**	**1,707**	**1,893**	**2,196**	**1,477**	**1,940**
Non-current liabilities							
Finance lease		–	–	14	–	–	14
Total non-current liabilities		**–**	**–**	**14**	**–**	**–**	**14**
Total liabilities		**2,659**	**1,707**	**1,907**	**2,196**	**1,477**	**1,954**
Net assets		**21,688**	**24,374**	**4,982**	**21,652**	**24,401**	**4,991**
Equity							
Share capital	6	49,757	44,903	17,092	49,757	44,912	17,092
Accumulated losses		(28,047)	(20,560)	(12,110)	(28,105)	(20,511)	(12,101)
Foreign currency translation reserve	6	(22)	31	–	–	–	–
		21,688	**24,374**	**4,982**	**21,652**	**24,401**	**4,991**

The accompanying notes form an integral part of these financial statements

XERO LIMITED – STATEMENTS OF CASH FLOWS – FOR THE YEAR ENDED 31 MARCH 2011

	Notes	Group 2011 ($000s)	Group 2010 ($000s)	Parent 2011 ($000s)	Parent 2010 ($000s)
Operating activities					
Cash was provided from					
Receipts from customers		8,615	2,851	8,308	2,300
GST received		136	64	39	48
Other income		362	123	325	123
Interest received		898	881	896	880
		10,011	**3,919**	**9,568**	**3,351**
Cash was applied to					
Payments to suppliers & employees		(15,231)	(10,714)	(14,934)	(10,308)
		(15,231)	**(10,714)**	**(14,934)**	**(10,308)**
Net cash flows from operating activities	15	**(5,220)**	**(6,795)**	**(5,366)**	**(6,957)**
Investing activities					
Cash was applied to					
Purchase of property, plant & equipment		(307)	(198)	(237)	(139)
Capitalised development costs		(2,752)	(1,749)	(2,747)	(1,749)
Intangible assets		(18)	(33)	(8)	(8)
Other assets		(18)	–	–	–
Investment in subsidiary		–	–	(67)	–
Investment in associate		(200)	–	(200)	–
Net cash flows from investing activities		**(3,295)**	**(1,980)**	**(3,259)**	**(1,896)**
Financing activities					
Cash was provided from					
Share buyback		–	(740)	–	(740)
Share issue		4,000	28,046	4,000	28,046
		4,000	**27,306**	**4,000**	**27,306**
Cash was applied to					
Refund/(cost) of share issue		40	(915)	40	(915)
Finance lease repayments		–	(20)	–	(20)
		40	**(935)**	**40**	**(935)**
Net cash flows from financing activities		**4,040**	**26,371**	**4,040**	**26,371**
Net (decrease) / increase in cash held		**(4,475)**	**17,596**	**(4,585)**	**17,518**
Foreign currency translation adjustment		–	(6)	–	(2)
Cash & cash equivalents at beginning of the year	10	21,397	3,807	21,236	3,720
Cash & cash equivalents at end of the year	10	**16,922**	**21,397**	**16,651**	**21,236**

The accompanying notes form an integral part of these financial statements

NOTES TO THE FINANCIAL STATEMENTS

1. CORPORATE INFORMATION

Xero Limited is a limited liability company, domiciled and incorporated in New Zealand and registered under the New Zealand Companies Act 1993. The registered office of the Company is Level 1, Old Bank, 98 Customhouse Quay, Wellington 6011, New Zealand.

The financial statements presented are for Xero Limited (the "Company") and its subsidiaries comprising Xero (UK) Limited, Xero Pty Limited (Australia), Xero Inc. (United States) and Xero Trustee Limited (together "the Group") for the year ended 31 March 2011.

Xero Limited is an issuer for the purposes of the Financial Reporting Act 1993.

The consolidated financial statements of the Group for the year ended 31 March 2011 were authorised for issue in accordance with a resolution of the Directors on 19 May 2011.

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

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(a) Basis of preparation The financial statements have been prepared in accordance with New Zealand Generally Accepted Accounting Practice. They comply with New Zealand Equivalents to International Financial Reporting Standards ("NZ IFRS"), and other applicable Financial Reporting Standards, as appropriate for profit-oriented entities. The financial statements comply with International Financial Reporting Standards ("IFRS").

The financial statements have been prepared in accordance with the requirements of the Financial Reporting Act 1993 and Companies Act 1993.

The Company and Group are profit-oriented companies for financial reporting purposes.

The consolidated financial statements have been prepared using the historical cost convention.

The preparation of financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements, are disclosed in Note 3.

(b) Changes in accounting policy & disclosures The accounting policies adopted are consistent with those of the previous year.

(c) Basis of consolidation Subsidiaries are all entities over which the Group has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases. The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Inter-company transactions, balances and unrealised gains on transactions between Group companies are eliminated. Unrealised losses are also eliminated. Accounting policies of subsidiaries are consistent with the policies adopted by the Group.

(d) Associates Associates are all entities over which the Group has significant influence but not control. Investments in associates are accounted for using the equity method of accounting and are initially recognised at cost.

The Group's share of its associates' post-acquisition profits or losses is recognised in the Income Statement, and its share of post acquisition movements in other comprehensive income is recognised in other comprehensive income. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment. When the Group's share of losses in an associate equals or exceeds its interest in the associate, including any other unsecured receivables, the Group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the associate.

Unrealised gains on transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associates. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of associates have been changed where necessary to ensure consistency with the policies adopted by the Group.

(e) Revenue Revenue in relation to subscriptions and training is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. Revenue is recorded net of GST and discounts and after eliminating sales within the Group. The following specific recognition criteria must also be met before revenue is recognised:

Services – Revenue is recognised in the accounting period in which the service is rendered. Consideration received prior to the service being rendered is recognised in the Statement of Financial Position as income in advance and included within trade and other payables. Revenue for which services have been rendered but invoices have not been issued is recognised within the Income Statement and in the Statement of Financial Position as accrued income within trade and other receivables.

Interest – Interest income is recognised on an accruals basis using the effective interest rate method.

Government grants – Government grants are recognised at their fair value where there is reasonable assurance that the grants will be received and all attaching conditions will be complied with. When a grant relates to an expense item, it is recognised as income over the period necessary to match the grant on a systematic basis to the costs that it is intended to compensate.

(f) Income tax Income tax expense comprises current and deferred tax. Income tax expense is recognised in the Income Statement except to the extent that it relates to items recognised directly in the Statement of Comprehensive Income or equity, in which case it is recognised in the Statement of Comprehensive Income or equity.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantially enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognised, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the reporting date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

A deferred tax asset is recognised to the extent that it is probable that future taxable profits will be available against which temporary differences can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related benefits will be realised. As permitted by NZIAS 12: Income Taxes, deferred tax assets in relation to tax losses have been recognised to the extent of the Group's deferred tax liabilities.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries and associates, except for deferred income tax liabilities where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income tax assets and liabilities relate to income tax levied by the same taxation authority on either the same taxable entity or different entities where there is an intention to settle the balance on a net basis.

(g) GST The Income Statement and the Statement of Cash Flows have been prepared so that all components are stated exclusive of GST, except where GST is not recoverable. All items in the Statement of Financial Position are stated net of GST with the exception of receivables and payables, which include GST invoiced.

Commitments and contingencies are disclosed net of the amount of GST recoverable from, or payable to, the taxation authority.

(h) Foreign currency translation 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"). The consolidated financial statements are presented in New Zealand dollars ($), which is the Company's functional currency. Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the Income Statement. Foreign exchange gains and losses are presented in the Income Statement within operating expenses.

The Group translates the results of its foreign operations from their functional currency to the presentation currency of the Group using the closing exchange rate at balance date for assets and liabilities and the average yearly exchange rate for the income and expenses. The difference arising from translation of the Statement of Financial Position at closing rate and the Income Statement at average rate is recorded within the Foreign Currency Translation Reserve.

(i) Property, plant & equipment Property, plant and equipment is stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Depreciation on assets is calculated using the straight-line method to allocate their costs to their residual values over their estimated useful lives, as follows:

Leasehold improvements	Terms of lease
Motor vehicles	3 – 4 years
Furniture & equipment	1 – 7 years
Computer equipment	2 – 3 years

The assets' residual values and useful lives are reviewed and adjusted if appropriate at each balance date.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

Gains and losses on disposals are determined by comparing proceeds with carrying amounts, and are recognised in the Income Statement.

(j) Intangible assets

(I) Research costs are expensed as incurred.

Costs associated with maintaining internal computer software programs are recognised as an expense as incurred. Costs that are directly associated with the development of identifiable and unique software products controlled by the Group 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.

Directly attributable costs that are capitalised as part of the capitalised software development costs include the software development employee costs. Other development expenditures that do not meet these criteria are recognised as expenses as incurred. Development costs previously recognised as expenses are not recognised as assets in a subsequent period. Computer software development costs recognised as assets are amortised over their estimated useful lives.

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

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.

(III) 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:

Trademarks / patents	10 years
Domains	10 years
Capitalised development costs	3-5 years (2010: 3-4 years)

(k) Impairment of non-financial assets 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.

Recoverable amount is the greater of fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Non-financial assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at each reporting date.

(l) Non-derivative financial instruments The Group classifies its financial assets as loans and receivables. The classifications depend on the purposes for which the financial assets were acquired. Management determines the classifications of its financial assets at initial recognition.

(m) Loans & receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets, except for those with maturities greater than 12 months after the reporting date. These are classified as non-current assets. The Group's loans and receivables comprise "trade & other receivables" and "cash & cash equivalents" in the Statement of Financial Position. Loans and receivables are carried at amortised cost using the effective interest method. The Group assesses at each reporting date whether there is objective evidence that a financial asset or a group of financial assets is impaired. Impairment testing of trade receivables is described in Note 2.(o). The Group does not have any derivatives.

(n) Cash & cash equivalents include cash in hand, deposits held at call with banks, other short-term, highly liquid investments with original maturities of three months or less, and bank overdrafts.

(o) Trade & other receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of trade receivables is established 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 an allowance account, and the amount of the loss is recognised in the Income Statement. When a trade receivable is uncollectible, it is written off against the allowance account for trade receivables. Subsequent recoveries of amounts previously written off are credited against the Income Statement.

(p) Trade & other payables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method. They represent liabilities for goods and services provided to the Group prior to the end of the financial year that are unpaid. The amounts are unsecured, non-interest bearing and are usually paid within 45 days of recognition.

(q) Employee entitlements The liability for employees' compensation for future leave is accrued in relation to the length of service rendered by employees and relates to the vested and unvested entitlements.

The Group operates both short-term and long-term incentive plans. Employee incentive obligations are measured on an undiscounted basis (short-term) and are expensed as the related service is provided. The Group operates an equity-settled, share-based compensation plan, under which the entity receives services from employees as consideration for equity instruments of the Group. The value of the employee services received for the grant of shares is recognised as an expense over the vesting period and the amount is determined by reference to the fair value of the shares granted.

(r) Leases Operating lease payments are recognised as an expense in the Income Statement on a straight-line basis over the lease term.

Finance leases, which transfer to the Group substantially all the risks and benefits incidental to ownership of the leased items, are capitalised at the inception of the leases at the fair value of the leased assets or, if lower, at the present value of the minimum lease payments. The leased assets and corresponding liabilities are therefore recognised and the assets are depreciated in line with the Group's depreciation policy to reflect estimated useful lives.

Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are included in the Income Statement as interest costs.

(s) 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 Group profit or loss attributable to ordinary shareholders of the Company by the weighted average number of ordinary shares outstanding during the period.

Diluted EPS is determined by adjusting the profit or loss attributable to ordinary shareholders and the weighted average number of ordinary shares outstanding for the effects of all dilutive potential ordinary shares, which comprise convertible notes and share options granted to employees.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(t) Share capital Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new shares are shown in equity as a deduction, net of tax, from the proceeds. Where any Group company purchases the Company's equity share capital (treasury shares), the consideration paid is deducted from equity attributable to the Company's equity holders until the shares are cancelled or transferred outside the Group.

(u) Segment reporting An operating segment is a component of an entity that engages in business activities from which it may earn revenue and incur expenses, whose operating results are regularly reviewed by the entity's Chief Operating Decision Maker to make decisions about resources to be allocated to the segment and assesses its performance, and for which discrete financial information is available. Operating segments are aggregated for disclosure purposes where they have similar products and services, production processes, customers, distribution methods and regulatory environments.

(v) Standards or interpretations issued but not yet effective
The following standards not yet effective are relevant to the Company and Group.

NZ IFRS 9 Financial Instruments – Recognition and Measurement of Financial Assets was issued in November 2009 as part of the IASB's project to replace IAS 39 Financial Instruments: Recognition and Measurement. The standard deals with accounting for financial assets, their recognition, derecognition and measurement. Financial assets are classified according to their measurement, either at fair value or amortised cost. The standard is effective for annual periods beginning on or after 1 January 2013. It is not expected to have a material impact on the Company or Group.

There are a number of other amendments to accounting standards as part of the ongoing improvement process. None of these changes is expected to impact significantly on the Group.

The Company or Group has not adopted any standards prior to their effective date.

3. SIGNIFICANT ACCOUNTING JUDGEMENTS

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.

(a) Deferred tax asset Deferred tax benefits relating to carry forward tax losses and deductible temporary differences are recognised by the Group and Company to the extent that it is probable that taxable profits will be available against which those losses and temporary differences can be recognised. Deferred tax assets in relation to tax losses have been recognised to the extent of the Group's deferred tax liabilities.

The Group has not recognised deferred tax benefits in relation to all carry forward losses as it is not considered probable that these losses will reverse in the foreseeable future. The Company has not yet reached break-even and is expected to make a further loss in the year ending 31 March 2012. It is not considered prudent to recognise a deferred tax asset in respect of losses and other temporary differences until the point that the Company reaches break-even.

(b) Capitalised development costs The Group capitalises its development costs based on a proportion of employee costs. The percentages applied are in line with industry standards. The Group regularly reviews the carrying value of capitalised development costs to ensure they are supported by the associated future economic benefits. The development costs are amortised over three to five years, being the expected useful life of the software (2010: three to four years).

The Group took the decision to change the amortisation rate from three to four years to three to five years as it considers this period to reflect better the period in which the capitalised development costs will generate future economic benefits.

The impact of the change in the useful life of capitalised development costs from three to four years to three to five years is a decrease in the amortisation cost for the year of $880,000.

4. REVENUES & EXPENSES

	Notes	Group 2011 ($000s)	Group 2010 ($000s)	Parent 2011 ($000s)	Parent 2010 ($000s)
Operating revenue from the rendering of services		**9,341**	**3,158**	**8,858**	**3,868**
Other income					
Government grants*		52	101	52	101
Research & development tax credit		273	–	273	–
Other		–	136	–	136
		325	**237**	**325**	**237**
Total operating revenue & other income		**9,666**	**3,395**	**9,183**	**4,105**
Operating expenses					
Employee entitlements		8,498	6,503	6,107	4,771
Advertising & marketing		2,237	1,282	1,490	823
IT infrastructure costs**		2,046	490	2,046	490
Inter company market support payments	17	–	–	3,644	3,502
Consulting & sub-contracting		412	325	368	240
Travel related		537	497	339	305
Lease/rental		472	368	433	342
Communication & office administration		325	287	246	215
Directors' fees		222	215	222	215
Fees paid to auditors	13	143	181	99	146
Loss on disposal of property, plant & equipment		–	3	–	3
Loss/(gain) on foreign exchange transactions		(40)	59	15	59
Other operating expenses		2,012	1,256	1,523	1,036
Total operating expenses exc. depreciation & amortisation		**16,864**	**11,466**	**16,532**	**12,147**
Depreciation & amortisation expense					
Property, plant & equipment	8	207	198	186	186
Amortisation of other intangible assets	9	10	6	7	6
Amortisation of development costs	9	936	1,204	930	1,204
Total depreciation & amortisation		**1,153**	**1,408**	**1,123**	**1,396**
Total operating expenses		**18,017**	**12,874**	**17,655**	**13,543**
Interest					
Interest income – bank		868	1,017	866	1,016
Interest income – loan to related party	17	8	12	8	12
Interest income – other		4	–	4	–
Net interest income		**880**	**1,029**	**878**	**1,028**
Net operating loss before tax		**(7,471)**	**(8,450)**	**(7,594)**	**(8,410)**

**Government grants have been received from New Zealand Trade and Enterprise in respect of overseas market development. The grants were claimed retrospectively on qualifying expenditure, and all conditions have been fulfilled at balance date.*

***Increase due to increased customer numbers and the introduction of Akamai services.*

5. CURRENT & DEFERRED INCOME TAX

Current income tax

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

	Group 2011 ($000s)	Group 2010 ($000s)	Parent 2011 ($000s)	Parent 2010 ($000s)
Accounting loss before income tax	(7,461)	(8,450)	(7,594)	(8,410)
At the statutory income tax rate of 30% (2010: 30%)	(2,238)	(2,535)	(2,278)	(2,523)
Non-deductible expenditure	20	21	11	13
Tax rate variance of subsidiary	(3)	–	–	–
Tax expense on share of associate company profit	3	–	–	–
Total tax losses not recognised	2,244	2,514	2,267	2,510
Income tax expense reported in Income Statement	**26**	**–**	**–**	**–**
Comprising				
Income tax	61	–	–	–
Deferred tax	(35)	–	–	–
Income tax expense	**26**	**–**	**–**	**–**
Opening balance	–	–	–	–
Income tax liability for the year	61	–	–	–
Income tax paid	–	–	–	–
Current tax payable	**61**	**–**	**–**	**–**

Imputation credit account

	Group 2011 ($000s)	Group 2010 ($000s)	Parent 2011 ($000s)	Parent 2010 ($000s)
Balance as at 1 April	–	–	–	–
New Zealand income tax payments during the year	–	–	–	–
Tax refunds received	–	–	–	–
Balance at 31 March	**–**	**–**	**–**	**–**

Deferred income tax

	Provisions ($000s)	Accelerated Depreciation ($000s)	Tax losses ($000s)	Net ($000s)
Group – Deferred tax asset/(liability) balances				
At 1 April 2010	–	–	–	–
Charged to income statement	296	(571)	310	35
At 31 March 2011	**296**	**(571)**	**310**	**35**
Parent – Deferred tax asset/(liability) balances				
At 1 April 2010	–	–	–	–
Charged to income statement	261	(571)	310	–
At 31 March 2011	**261**	**(571)**	**310**	**–**

It is not anticipated that deferred tax balances will be recovered within 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 $26,698,000 (2010: $18,675,000) subject to shareholder continuity being maintained as required by New Zealand tax legislation.

6. SHARE CAPITAL

Movement in ordinary shares on issue

	Notes	Group 2011 (000s)	Group 2010 (000s)	Parent 2011 (000s)	Parent 2010 (000s)
Balance as at 1 April		87,631	55,460	87,640	55,460
Issue of ordinary shares		2,681	32,273	2,681	32,273
Issue of ordinary shares for employee restricted share plan		700	–	691	–
Ordinary shares on issue at 31 March		**91,012**	**87,733**	**91,012**	**87,733**
Treasury stock	19	763	522	763	513
Ordinary shares on issue at 31 March		**90,249**	**87,211**	**90,249**	**87,220**

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

The Company issued 0.6 million shares in June 2010 as part of the Company's Employee Restricted Share Plan at an average price of $1.44. In October 2010 the Company undertook a share placement whereby a total of 2.7 million new shares were issued at $1.4918.

Included within the value of share capital in 2011 are transaction costs associated with the issue of 3.3 million ordinary shares that took place in June and October 2010 and a receipt of a refund of GST on prior year overseas issue costs from the IRD. These transaction costs were directly associated with the equity transactions and accordingly have been accounted for as a deduction from equity.

Treasury stock includes shares issued in relation to the Employee Restricted Share Plan that have yet to vest.

Foreign currency translation reserve

	Group 2011 ($000s)	Group 2010 ($000s)	Parent 2011 ($000s)	Parent 2010 ($000s)
Balance as at 1 April	31	–	–	–
Translation of overseas subsidiaries into presentation currency	(53)	31	–	–
Balance as at 31 March	**(22)**	**31**	**–**	**–**

Capital risk management The Group's objectives when managing capital (comprising share capital) are to safeguard the Group's ability to continue as a going concern in order to provide returns for shareholders, and to maintain an optimal capital structure.

7. EARNINGS PER SHARE

Loss attributable to ordinary shareholders

	Notes	Group 2011 (000s)	Group 2010 (000s)	Parent 2011 (000s)	Parent 2010 (000s)
Net loss after tax		($7,487)	($8,450)	($7,594)	($8,410)
Issued ordinary shares	6	91,012	87,733	91,012	87,733
Weighted average of issued ordinary shares		89,322	83,455	89,322	83,464
Basic & diluted loss per share		($0.08)	($0.10)	($0.09)	($0.10)

The prior period restatement of the Employee Restricted Share Plan (refer Note 23) has no impact on the Earnings per Share.

8. PROPERTY, PLANT & EQUIPMENT

	Leasehold improvements ($000s)	Motor vehicles ($000s)	Computer equipment ($000s)	Furniture & equipment ($000s)	Total ($000s)
Group – Year ended 31 March 2011					
Cost					
Balance as at 1 April 2010	255	60	422	162	899
Additions	53	20	144	90	307
Disposals	–	–	–	–	–
Foreign exchange adjustment	–	–	(1)	–	(1)
Balance as at 31 March 2011	**308**	**80**	**565**	**252**	**1,205**
Depreciation					
Balance as at 1 April 2010	125	48	282	77	532
Depreciation expense	57	14	109	27	207
Disposals	–	–	–	–	–
Balance as at 31 March 2011	**182**	**62**	**391**	**104**	**739**
Net carrying amount	**126**	**18**	**174**	**148**	**466**
Parent – Year ended 31 March 2011					
Cost					
Balance as at 1 April 2010	255	60	379	155	849
Additions	51	20	108	58	237
Disposals	–	–	–	–	–
Balance as at 31 March 2011	**306**	**80**	**487**	**213**	**1,086**
Depreciation					
Balance as at 1 April 2010	125	48	266	77	516
Depreciation expense	57	14	91	24	186
Disposals	–	–	–	–	–
Balance as at 31 March 2011	**182**	**62**	**357**	**101**	**702**
Net carrying amount	**124**	**18**	**130**	**112**	**384**

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	Leasehold improvements ($000s)	Motor vehicles ($000s)	Computer equipment ($000s)	Furniture & equipment ($000s)	Total ($000s)
Group – Year ended 31 March 2010					
Cost					
Balance as at 1 April 2009	246	60	290	126	722
Additions	9	–	148	41	198
Disposals	–	–	(14)	(5)	(19)
Foreign exchange adjustment	–	–	(2)	–	(2)
Balance as at 31 March 2010	**255**	**60**	**422**	**162**	**899**
Depreciation					
Balance as at 1 April 2009	82	28	183	54	347
Depreciation expense	43	20	109	26	198
Disposals	–	–	(9)	(3)	(12)
Foreign exchange adjustment	–	–	(1)	–	(1)
Balance as at 31 March 2010	**125**	**48**	**282**	**77**	**532**
Net carrying amount	**130**	**12**	**140**	**85**	**367**
Parent – Year ended 31 March 2010					
Cost					
Balance as at 1 April 2009	246	60	274	125	705
Additions	9	–	116	35	160
Disposals	–	–	(11)	(5)	(16)
Balance as at 31 March 2010	**255**	**60**	**379**	**155**	**849**
Depreciation					
Balance as at 1 April 2009	82	28	177	54	341
Depreciation expense	43	20	97	26	186
Disposals	–	–	(8)	(3)	(11)
Balance as at 31 March 2010	**125**	**48**	**266**	**77**	**516**
Net carrying amount	**130**	**12**	**113**	**78**	**333**

9. INTANGIBLE ASSETS

	Patents & trademarks ($000s)	Software development* ($000s)	Domains ($000s)	Total ($000s)
Group – Year ended 31 March 2011				
Cost				
Balance as at 1 April 2010	22	4,935	70	5,027
Additions	7	2,753	11	2,771
Balance as at 31 March 2011	**29**	**7,688**	**81**	**7,798**
Amortisation & impairment				
Balance as at 1 April 2010	5	2,061	13	2,079
Amortisation during the year**	2	936	8	946
Balance as at 31 March 2011	**7**	**2,997**	**21**	**3,025**
Net carrying amount	**22**	**4,691**	**60**	**4,773**
Parent – Year ended 31 March 2011				
Cost				
Balance as at 1 April 2010	22	4,935	45	5,002
Additions	4	2,747	4	2,755
Balance as at 31 March 2011	**26**	**7,682**	**49**	**7,757**
Amortisation & impairment				
Balance as at 1 April 2010	5	2,061	13	2,079
Amortisation during the year**	2	930	5	937
Balance as at 31 March 2011	**7**	**2,991**	**18**	**3,016**
Net carrying amount	**19**	**4,691**	**31**	**4,741**
Group – Year ended 31 March 2010				
Cost				
Balance as at 1 April 2009	18	2,839	70	2,927
Additions	4	2,096	–	2,100
Balance as at 31 March 2010	**22**	**4,935**	**70**	**5,027**
Amortisation & impairment				
Balance as at 1 April 2009	3	857	9	869
Amortisation during the year	2	1,204	4	1,210
Balance as at 31 March 2010	**5**	**2,061**	**13**	**2,079**
Net carrying amount	**17**	**2,874**	**57**	**2,948**

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	Patents & trademarks ($000s)	Software development* ($000s)	Domains ($000s)	Total ($000s)
Parent – Year ended 31 March 2010				
Cost				
Balance as at 1 April 2009	18	2,839	41	2,898
Additions	4	2,096	4	2,104
Balance as at 31 March 2010	**22**	**4,935**	**45**	**5,002**
Amortisation & impairment				
Balance as at 1 April 2009	3	857	9	869
Amortisation during the year	2	1,204	4	1,210
Balance as at 31 March 2010	**5**	**2,061**	**13**	**2,079**
Net carrying amount	**17**	**2,874**	**32**	**2,923**

**Capitalised development costs have been internally generated.*

***The Group took the decision to change the amortisation rate from three to four years to three to five years as it considers this period to better reflect the period in which the capitalised development costs will generate future economic benefits. The impact of the change in the useful life of capitalised development costs from three to four years to three to five years is a decrease in the amortisation cost for the year of $880,000.*

10. CASH & CASH EQUIVALENTS

	Group 2011 ($000s)	Group 2010 ($000s)	Parent 2011 ($000s)	Parent 2010 ($000s)
Cash at bank	380	597	151	436
Bank term deposits	16,542	20,800	16,500	20,800
	16,922	**21,397**	**16,651**	**21,236**

11. TRADE & OTHER RECEIVABLES

	Notes	Group 2011 ($000s)	Group 2010 ($000s)	Parent 2011 ($000s)	Parent 2010 ($000s)
Current assets					
Trade receivables		814	536	587	384
Trade receivables from related parties	17	–	–	122	–
Accrued income		350	–	221	–
Prepayments		172	178	90	156
Interest receivable		167	197	167	197
Government grant receivable		–	37	–	37
GST receivable		–	10	–	6
		1,503	**958**	**1,187**	**780**
Non-current assets					
Loans to Directors	17	232	336	232	336
NZX bond		75	75	75	75
Other loans		116	–	116	–
Other assets		18	–	–	–
		441	**411**	**423**	**411**

Trade receivables that are less than three months past due are not considered impaired. As of 31 March 2011, trade receivables of the Parent and Group of $24,000 were past due (2010: $30,000). These relate to a number of independent customers for whom there is no recent history of default. The Group has no impaired receivables.

12. TRADE & OTHER PAYABLES

	Notes	Group 2011 ($000s)	Group 2010 ($000s)	Parent 2011 ($000s)	Parent 2010 ($000s)
Trade payables		915	491	768	401
Trade payables due to related parties	*17*	–	–	207	304
Other payables & accrued expenses		478	214	265	120
Income in advance		–	98	–	41
GST payable		145	19	33	–
Income tax payable	*5*	61	–	–	–
Employee entitlements		1,060	885	923	611
		2,659	**1,707**	**2,196**	**1,477**

13. AUDITORS' REMUNERATION

	Group 2011 ($000s)	Group 2010 ($000s)	Parent 2011 ($000s)	Parent 2010 ($000s)
Amounts received or due & receivable by PricewaterhouseCoopers for:				
Audit of financial statements	86	72	42	37
Other assurance services in relation to the entity*	19	23	19	23
Taxation services**	38	86	38	86
Total fees paid to auditors	**143**	**181**	**99**	**146**

**Other assurance services relate to agreed upon procedures over the Group's half year result and the audit of the Company's share register.*
***Taxation services primarily relate to the provision of assurance services for the annual tax return.*

14. FINANCIAL INSTRUMENTS & FINANCIAL RISK MANAGEMENT OBJECTIVES

Financial instruments Financial instruments recognised in the Statement of Financial Position include cash balances, receivables and payables. It is, and has been, through the period of these financial statements, the Group's policy that no trading in financial instruments shall be undertaken.

Classification & fair values The carrying value of the Parent's and Group's financial instruments approximates their fair value. Set out below is a comparison by category of the carrying amounts of all the Parent's and Group's financial instruments and their fair values.

	Loans & receivables ($000s)	Financial liabilities at amortised cost ($000s)	Total carrying value ($000s)	Fair value ($000s)
Group – Year ended 31 March 2011				
Assets				
Trade & other receivables	981	–	981	981
Cash & cash equivalents	16,922	–	16,922	16,922
Loans to Directors	232	–	232	232
Other loans	134	–	134	134
Total financial assets	**18,269**	–	**18,269**	**18,269**
Liabilities				
Trade & other payables	–	1,393	1,393	1,393
Total financial liabilities	–	**1,393**	**1,393**	**1,393**
Group – Year ended 31 March 2010				
Assets				
Trade & other receivables	770	–	770	770
Cash & cash equivalents	21,397	–	21,397	21,397
Loans to Directors	336	–	336	336
Total financial assets	**22,503**	–	**22,503**	**22,503**
Liabilities				
Trade & other payables	–	705	705	705
Total financial liabilities	–	**705**	**705**	**705**
Parent – Year ended 31 March 2011				
Assets				
Trade & other receivables	876	–	876	876
Cash & cash equivalents	16,651	–	16,651	16,651
Loans to Directors	232	–	232	232
Other loans	116	–	116	116
Total financial assets	**17,875**	–	**17,875**	**17,875**
Liabilities				
Trade & other payables	–	1,240	1,240	1,240
Total financial liabilities	–	**1,240**	**1,240**	**1,240**

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	Loans & receivables ($000s)	Financial liabilities at amortised cost ($000s)	Total carrying value ($000s)	Fair value ($000s)
Parent – Year ended 31 March 2010				
Assets				
Trade & other receivables	618	–	618	618
Cash & cash equivalents	21,236	–	21,236	21,236
Loans to Directors	336	–	336	336
Total financial assets	**22,190**	**–**	**22,190**	**22,190**
Liabilities				
Trade & other payables	–	825	825	825
Total financial liabilities	**–**	**825**	**825**	**825**

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 balances. These are placed on deposit at variable rates which expose the Group to cash flow interest rate risk. The Group does not enter into forward rate agreements or any interest rate hedges.

The Company's management regularly reviews its banking arrangements to ensure that it achieves the best returns on its funds while maintaining access to necessary cash levels to service the Company's day-to-day activities.

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

	Interest rate	Balance sheet ($000s)	12 months ($000s)	24 months ($000s)	>24 months ($000s)
Group – Year ended 31 March 2011					
Financial assets					
Cash at bank	4.9%	16,922	16,922	–	–
Loans to Directors	4.0%	232	–	232	–
Other loans	4.0%	116	–	116	–
Other assets	5.5%	18	–	18	–
Total		**17,288**	**16,922**	**366**	**–**
Parent – Year ended 31 March 2011					
Financial assets					
Cash at bank	4.9%	16,651	16,651	–	–
Loans to Directors	4.0%	232	–	232	–
Other loans	4.0%	116	–	116	–
Total		**16,999**	**16,651**	**348**	**–**
Group – Year ended 31 March 2010					
Financial assets					
Cash at bank	4.5%	21,397	21,397	–	–
Loans to Directors	4.0%	336	–	–	336
Total		**21,733**	**21,397**	**–**	**336**

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14. FINANCIAL INSTRUMENTS & FINANCIAL RISK MANAGEMENT OBJECTIVES (CONTINUED)

	Interest rate	Balance sheet ($000s)	12 months ($000s)	24 months ($000s)	>24 months ($000s)
Parent – Year ended 31 March 2010					
Financial assets					
Cash at bank	5.9%	21,236	21,236	–	–
Loans to Directors	4.0%	336	–	–	336
Total		**21,572**	**21,236**	**–**	**336**

Of the financial assets and liabilities above, only the Cash at bank is subject to floating interest rate risk. Loans to Directors and other loans are subject to fixed rate interest. All other financial assets and liabilities of the Group are not subject to interest rate risk.

As at 31 March 2011 if interest rates had been 2.0% higher/lower with all other variables held constant, interest income, net loss and retained earnings for the Company and the Group would have decreased/increased by $371,000 (2010: $496,000).

Liquidity risk Liquidity risk is the risk that the Company or Group cannot pay contractual liabilities as they fall due. During the year, the Company raised $4.0 million by way of private placement. Following the receipt of the private placement funds, the Company has sufficient cash to meet its requirements in the foreseeable future. The Group has no debt and therefore management remains focused on generating sufficient revenue from sales to cover the ongoing costs of operation.

The following table sets out the undiscounted contractual cash flows for all financial liabilities of the Company and Group:

	Balance sheet ($000s)	Contractual cash flows ($000s)	6 months or less ($000s)	6–12 months ($000s)	1–2 years ($000s)	More than 2 years ($000s)
Group – Year ended 31 March 2011						
Trade payables	1,393	1,393	1,393	–	–	–
Total non-derivative liabilities	**1,393**	**1,393**	**1,393**	**–**	**–**	**–**
Parent – Year ended 31 March 2011						
Trade payables	1,240	1,240	1,240	–	–	–
Total non-derivative liabilities	**1,240**	**1,240**	**1,240**	**–**	**–**	**–**
Group – Year ended 31 March 2010						
Trade payables	705	705	705	–	–	–
Total non-derivative liabilities	**705**	**705**	**705**	**–**	**–**	**–**
Parent – Year ended 31 March 2010						
Trade payables	825	825	825	–	–	–
Total non-derivative liabilities	**825**	**825**	**825**	**–**	**–**	**–**

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 bank balances and receivables.

The Group manages its exposure to credit risk by monitoring the credit quality of the financial institutions that hold its cash balances. The credit risk associated with trade receivables is small because of the inherently low individual transaction value and the spread over many customers.

Continued on next page ...

Maximum exposure to credit risk at balance date

	Group 2011 ($000s)	Group 2010 ($000s)	Parent 2011 ($000s)	Parent 2010 ($000s)
Cash & cash equivalents	16,922	21,397	16,651	21,236
Receivables	981	770	876	618
Non-current receivables	366	336	348	336
Total	**18,269**	**22,503**	**17,875**	**22,190**

Foreign currency risk The Group faces the risk of movements in foreign currency exchange rates against the New Zealand dollar. The Group operates in three other currencies, being UK pounds, Australian dollars and US dollars. As a result the Group's Income Statement and Statements of Financial Position can be affected by movements in exchange rates.

Both the UK and Australian operations are now self funding. The US operation is funded directly from New Zealand and will continue to require funding support for at least the next year. During this time the foreign currency risk will increasingly be mitigated by the generation of revenues in the US.

The potential effect on the Company's and Group's results if the New Zealand dollar weakens by 10% against the other operating currencies, with all other variables remaining constant, is an increase in the net loss and retained earnings for the Group by $122,000 (2010: $296,000).

15. RECONCILIATION OF OPERATING CASH FLOWS

	Group 2011 ($000s)	Group 2010 ($000s)	Parent 2011 ($000s)	Parent 2010 ($000s)
Reconciliation from the net (loss) after tax to the net cash from operating activities				
Net loss after tax	(7,487)	(8,450)	(7,594)	(8,410)
Adjustments				
Depreciation	207	198	186	186
Amortisation	946	1,210	937	1,210
Deferred tax	(35)	–	–	–
Associated company profit	(7)	–	–	–
Translation of foreign operations	(53)	59	–	–
Employee entitlements	814	–	805	–
Interest on loans to directors	(8)	(12)	(8)	(12)
Interest on loans to others	(4)	–	(4)	–
Changes in working capital items				
(Increase)/decrease in trade receivables & prepayments	(545)	(680)	(407)	(547)
(Decrease)/increase in trade payables & accruals	688	359	415	356
(Decrease)/increase in GST	126	10	33	(5)
(Decrease)/increase in current tax	61	–	–	–
(Decrease)/increase in employee entitlements	175	498	312	282
(Decrease)/increase in income in advance	(98)	13	(41)	(17)
Net cash flows from operating activities	**(5,220)**	**(6,795)**	**(5,366)**	**(6,957)**

16. SEGMENT INFORMATION

The Group has three reporting segments based on the geographical locations of the operations and revenue streams.

These segments have been determined based on the reports reviewed by the Chief Operating Decision Maker to make strategic decisions.

The Group currently operates in one business segment, providing an online accounting solution for small businesses.

Sales between segments are carried out at arm's length. The revenue from external parties reported to the Board is measured in a manner consistent with that in the Income Statement. Entities are domiciled in New Zealand, the United Kingdom and Australia. Revenue from external customers is generated in their domiciliation countries, except for New Zealand where the total of revenue from other countries is $616,000 (2010: $195,000).

The total of non-current assets, other than financial instruments, located in New Zealand is $5,748,000 (2010: $3,645,000) and the total of non-current assets located in other countries is $139,000 (2010: $60,000).

	New Zealand ($000s)	United Kingdom ($000s)	Australia ($000s)	Inter-segment eliminations ($000s)	Total ($000s)
Group – Year ended 31 March 2011					
Total segment revenue	8,858	2,715	3,717	–	15,290
Inter-segment revenue	(2,305)	(1,421)	(2,223)	–	(5,949)
Revenue from external customers	6,553	1,294	1,494	–	9,341
Depreciation & amortisation	(1,123)	(9)	(21)	–	(1,153)
Interest revenue	878	–	2	–	880
Segment net (loss)/profit before tax	(7,594)	30	38	65	(7,461)
Segment net (loss)/profit after tax	(7,594)	23	19	65	(7,487)
Non-current asset additions	3,271	16	86	(58)	3,315
Segment assets	23,848	860	916	(1,277)	24,347
Segment liabilities	2,196	706	875	(1,118)	2,659
Group – Year ended 31 March 2010					
Total segment revenue	3,868	2,645	1,493	–	8,006
Inter-segment revenue	(1,346)	(2,292)	(1,210)	–	(4,848)
Revenue from external customers	2,522	353	283	–	3,158
Depreciation & amortisation	(1,396)	(6)	(6)	–	(1,408)
Interest revenue	1,028	–	1	–	1,029
Segment net (loss)/profit before & after tax	(8,410)	8	8	(56)	(8,450)
Non-current asset additions	2,264	15	49	–	2,328
Segment assets	25,878	1,153	1,107	(2,057)	26,081
Segment liabilities	1,477	1,040	1,034	(1,844)	1,707

17. RELATED PARTIES

The Company entered into the following transactions and had balances payable/receivable with the following related parties:

Xero (UK) Limited (United Kingdom)

	Group 2011 ($000s)	Group 2010 ($000s)	Parent 2011 ($000s)	Parent 2010 ($000s)
Market support payments to subsidiary	–	–	1,421	2,292
Distribution charge to subsidiary	–	–	985	1,018
Due to subsidiary	–	–	(140)	(218)

Xero Pty Limited (Australia)

	Group 2011 ($000s)	Group 2010 ($000s)	Parent 2011 ($000s)	Parent 2010 ($000s)
Market support payments to subsidiary	–	–	2,223	1,210
Distribution charge to subsidiary	–	–	1,319	353
Due from/(to) subsidiary	–	–	122	(95)

Xero Inc (United States)

	Group 2011 ($000s)	Group 2010 ($000s)	Parent 2011 ($000s)	Parent 2010 ($000s)
Operating revenue	–	–	–	–
Operating expense	–	–	–	–
Due to subsidiary	–	–	(67)	–

Xero Inc was incorporated on 24 February 2011 but did not trade for the period.

All transactions and outstanding balances with these related parties are priced on an arm's length basis and are to be settled in cash and under normal commercial terms. None of the balances are secured.

Operating revenue/(expense) includes management fees, distributor costs and market support payments between the Company and its subsidiaries.

Xero Trustee Limited

	Group 2011 ($000s)	Group 2010 ($000s)	Parent 2011 ($000s)	Parent 2010 ($000s)
Due from subsidiary in relation to shares issued during the year	–	–	–	9

Xero Trustee Limited was incorporated on 1 May 2008 to act as Trustee for the Xero Limited Employee Restricted Share Plan (Note 19). These balances represent forfeited shares held for future allocation.

The Group and Company entered into the following transactions and had balances payable/receivable with the following related parties:

Loans to Directors

	Loan 2011 ($000s)	Accumulated interest 2011 ($000s)	Balance outstanding 2011 ($000s)	Balance outstanding 2010 ($000s)
Guy Haddleton (Ceased to be a Director during the year)	–	–	–	112
Phil Norman	100	16	116	112
Graham Shaw	100	16	116	112
	200	**32**	**232**	**336**

Unsecured loans were issued to Directors during the year ended 31 March 2008 to purchase shares in the Company at $1.00 per share. Simple interest is accrued at a rate of 4%, with the loans and interest being repayable five years after the date of issue.

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17. RELATED PARTIES (CONTINUED)

Other related parties – key management & Directors

	Transaction value for year 2011 ($000s)	Transaction value for year 2010 ($000s)	Balance outstanding 2011 ($000s)	Balance outstanding 2010 ($000s)
Trade payables to related parties:				
Hamish Edwards – Openside CA Limited	21	6	–	–
Sam Morgan – Sonar 6	5	7	–	–
	26	**13**	–	–

All transactions and outstanding balances with these related parties are priced on an arm's length basis and are to be settled in cash and under normal commercial terms. Transactions relate to the provision of consultancy services by Openside and Sonar 6. None of the balances are secured.

Some members of key management and Directors subscribe to the Xero services provided by the Group. None of these related party transactions were significant to either the Company or the Directors.

Some members of key management participate in the Employee Restricted Share Plan (Note 19).

No amounts with any related parties have been written off or foregone during the year (2010: Nil).

Key management personnel remuneration 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 Chief Executive, his direct reports and Directors. The following table summarises remuneration paid to key management personnel.

	2011 ($000s)	2010 ($000s)
Short-term employee benefits	1,878	1,315
Share based payments (under the Employee Restricted Share Plan)	243	114

Key management personnel within 2011 include the country managers who now report to the Chief Executive.

18. COMMITMENTS & CONTINGENCIES

There are no capital commitments or contingent liabilities as at 31 March 2011 (2010: Nil).

19. EMPLOYEE RESTRICTED SHARE PLAN

In May 2008 the Xero Limited Employee Restricted Share Plan ('RSP') was introduced for selected executives and employees of the Group. Under the RSP, ordinary shares in Xero Limited are issued to Xero Trustee Limited, a wholly-owned subsidiary, and allocated to participants, on grant date, using funds lent to them by the Company.

Under the RSP, the shares are beneficially owned by the participants. The length of retention period before the shares vest is between one and three years. The price for each share issued during the year under the RSP is the higher of the volume-weighted average end-of-day market price reported on the New Zealand Exchange for the 20 business days immediately preceding the date on which the share is allocated or the invitation price.

If the individual is still employed by the Group at the end of this specific period, the employee is given a cash bonus that must be used to repay the loan and the shares are then transferred to the individual. The number of shares awarded is determined by the Remuneration Committee of the Board of Directors. The weighted average grant date fair value of restricted shares issued during the year was $1.44 (2010: $1.65). Shares with a grant date fair value of $483,000 vested during the year (2010: $268,000). The Group has no legal or constructive obligation to repurchase the shares or settle the RSP for cash.

Continued on next page ...

19. EMPLOYEE RESTRICTED SHARE PLAN (CONTINUED)

	Number of shares 2011 (000s)	Number of shares 2010 (000s)
Unvested shares as at 1 April	420	227
Awarded pursuant to RSP	721	476
Forfeited	(118)	(78)
Vested	(344)	(205)
Unvested shares as at 31 March	**679**	**420**
Forfeited shares not yet reallocated	84	102
	763	**522**
Percentage of total ordinary shares	0.8%	0.6%
Ageing of unvested shares		
Balance of shares to vest on 31 March 2012	358	205
Balance of shares to vest on 31 March 2013	321	215
	679	**420**

20. OPERATING LEASE COMMITMENTS FOR THE GROUP'S PREMISES

	Group 2011 ($000s)	Group 2010 ($000s)	Parent 2011 ($000s)	Parent 2010 ($000s)
Within one year	403	314	339	314
After one year but not more than five years	245	422	144	422
	648	**736**	**483**	**736**

21. INVESTMENT IN SUBSIDIARIES

Subsidiaries

	Country of incorporation	Balance date	Interest 2011 (%)	Interest 2010 (%)
Xero Inc	United States	31 December	100%	n/a
Xero Pty Limited	Australia	30 June	100%	100%
Xero Trustee Limited	New Zealand	31 March	100%	100%
Xero (UK) Limited (formerly Xero Live Limited)	United Kingdom	31 March	100%	100%

Xero Inc was incorporated on 24 February 2011 but did not trade for the period.
Xero Trustee Limited was incorporated on 1 May 2008 and is the Trustee for the Xero Limited Employee Restricted Share Plan.

22. INVESTMENT IN ASSOCIATE

	2011 ($000s)	2010 ($000s)
At 1 April	–	–
Acquisition of associate	200	–
Share of profit	10	–
Income tax expense	(3)	–
At 31 March	**207**	–

22. INVESTMENT IN ASSOCIATE (CONTINUED)

Xero Limited purchased 189 shares of Max Solutions Holdings Limited, an unlisted company, on 24 December 2010.

The Group's share of the results of its associate and its aggregated assets and liabilities is as follows:

Name	Country of incorporation	Assets ($000s)	Liabilities ($000s)	Revenues ($000s)	Profit ($000s)	Interest held
Max Solutions Holdings Limited	NZ	212	4	221	7	15.90%

Xero Limited has provided Max Solutions Holdings Limited with an unsecured debt facility of up to $100,000 that can be drawn down at any time until 31 March 2012. Interest is payable at OCR+5%. At 31 March 2011 no amounts had been drawn down.

23. PRIOR PERIOD RESTATEMENT OF EMPLOYEE RESTRICTED SHARE PLAN

In the prior year the Company treated the non-recourse loan to employees and the unvested cost of the Employee Restricted Share Plan as a receivable and accrual within the Statement of Financial Position. For the 2011 year the Company has determined that it is more appropriate to record these transactions as equity transactions. This classification is compliant with NZ IFRS. Comparative balances have been restated to reflect this change.

	31 March 2009 (as previously reported) ($000s)	Adjustment ($000s)	31 March 2009 (restated) ($000s)	31 March 2010 ($000s)	Adjustment ($000s)	31 March 2010 (restated) ($000s)
Group						
Assets						
Trade & other receivables – loans to employees	122	(122)	–	277	(277)	–
Non-current assets – loans to employees	106	(106)	–	314	(314)	–
Liabilities						
Trade & other payables – employee entitlements	(692)	190	(502)	(1,256)	371	(885)
Equity						
Treasury stock	–	228	228	147	591	738
Share based payments reserve	–	(190)	(190)	–	(371)	(371)
Parent						
Assets						
Trade & other receivables – loans to employees	122	(122)	–	277	(277)	–
Non-current assets – loans to employees	106	(106)	–	314	(314)	–
Liabilities						
Trade & other payables – employee entitlements	(634)	190	(444)	(982)	371	(611)
Equity						
Treasury stock	–	228	228	138	591	729
Share based payments reserve	–	(190)	(190)	–	(371)	(371)

24. EVENTS AFTER THE BALANCE SHEET DATE

On 6 May 2011 the Company entered into a long term agreement to lease new premises in Wellington. The lease will commence in March 2012.

AUDITORS' REPORT

We have audited the financial statements of Xero Limited on pages 4 to 30, which comprise the statements of financial position as at 31 March 2011, the income statements, statements of comprehensive income, statements of changes in equity and cash flow statements for the year then ended, and the notes to the financial statements that include a summary of significant accounting policies and other explanatory information for both the Company and the Group. The Group comprises the Company and the entities it controlled at 31 March 2011 or from time to time during the financial year.

Directors' Responsibility for the Financial Statements The Directors are responsible for the preparation of these financial statements in accordance with generally accepted accounting practice in New Zealand and that give a true and fair view of the matters to which they relate and for such internal controls as the Directors determine are necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing (New Zealand) and International Standards on Auditing. These 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 the auditors' 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, the auditor considers the internal controls relevant to the Company's and Group's preparation of financial statements that give a true and fair view of the matters to which they relate 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 Company's and Group'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 that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Other than in our capacity as auditors and providers of other assurance and taxation services, we have no relationship with, or interests in, Xero Limited or any of its subsidiaries. These services have not impaired our independence as auditors of the Company and Group.

Opinion In our opinion, the financial statements on pages 4 to 30:

(i) comply with generally accepted accounting practice in New Zealand;
(ii) comply with International Financial Reporting Standards; and
(ii) give a true and fair view of the financial position of the Company and Group as at 31 March 2011, and their financial performance and cash flows for the year then ended.

Report on Other Legal and Regulatory Requirements We also report in accordance with Sections 16(1)(d) and 16(1)(e) of the Financial Reporting Act 1993. In relation to our audit of the financial statements for the year ended 31 March 2011:

(i) we have obtained all the information and explanations that we have required; and
(ii) in our opinion, proper accounting records have been kept by the Company as far as appears from an examination of those records.

Restriction on Distribution or Use This report is made solely to the Company's shareholders, as a body, in accordance with Section 205(1) of the Companies Act 1993. Our audit work has been undertaken so that we might state to the Company's shareholders those matters which we are required to state to them in an auditors' 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.

PricewaterhouseCoopers

PricewaterhouseCoopers
Chartered Accountants
Wellington, New Zealand
19 May 2011

PRICEWATERHOUSECOOPERS

CORPORATE GOVERNANCE

The role of the Board The Board of Directors is elected by shareholders to govern Xero in their interests. The Board is the overall and final body responsible for all decision-making within the Company. The Board Charter describes the Board's role and responsibilities and regulates internal Board procedures.

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

Delegation of authority framework 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 clearly documented. The Chief Executive has, in some cases, formally delegated certain authorities to his direct reports and has established a formal process for his direct reports to sub-delegate certain authorities.

Membership size and composition The Board comprises seven Directors, being a non-executive Chairman, two Executive Directors and four non-executive Directors. The Board has a broad range of IT, financial, sales, business and other skills and expertise necessary to meet its objectives.

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

Director independence The Board Charter requires that a majority of Directors be "independent".

As required by the NZSX listing rules, Xero's approach to Director independence is to have regard to relationships that could (or could be perceived to) materially interfere with the exercise of the unfettered and independent judgement of a Director. The NZSX listing rules provide guidance as to the types of relationship that constitute "material relationships", affecting independence or the perception of independence.

The Board will review any determination it makes as to a Director's independence on becoming aware of any information that indicates the Director may have a relevant material relationship with Xero. For this purpose, Directors are required to ensure that they immediately advise of any new or changed relationships to enable the Board to consider and determine the materiality of the relationships.

The Board considers that Phil Norman, Graham Shaw, Sam Knowles and Sam Morgan are independent. The Board determined that Rod Drury and Hamish Edwards are not independent by virtue of their executive responsibilities. Further the Board considers that Craig Winkler is not independent.

Conflicts of interest The Board Charter outlines the Board's policy on conflicts of interest. Where conflicts of interest do exist at law, Directors excuse themselves from discussions and do not receive the relevant paper in respect of those interests, and in accordance with the relevant stock exchange listing rules do not exercise their right to vote in respect of such matters.

Nominations and appointment The procedures for the appointment and removal of Directors are ultimately governed by the Company's Constitution. The suitability of candidates for appointment is based on pre-established criteria. When recommending a candidate to act as Director, the Board takes into account such factors as it deems appropriate, including the experience, qualifications, availability and judgement of the candidate and the candidate's ability to work with other Directors.

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

Board Committees The Board operated three Committees during the year: the Audit and Risk Management Committee, the Remuneration Committee and the Nominations Committee. The Charters of each Committee are on the Xero website. The membership of each Committee is as follows:

1. Audit and Risk Management Committee
   - Graham Shaw (Chair), Sam Knowles, Sam Morgan, Phil Norman
2. Remuneration Committee
   - Phil Norman (Chair), Graham Shaw, Craig Winkler
3. Nominations Committee
   - Graham Shaw (Chair), Sam Knowles, Sam Morgan, Phil Norman, Craig Winkler

Retirement and re-election The Constitution provides that a Director is required to stand for re-election at the third Annual Meeting following the Director's appointment or three years, whichever is the longer.

Director remuneration Directors' fees have been previously set at $250,000 for the non-executive Directors. The fees paid for the past year were $221,989.

Board access to information and advice The Directors generally receive materials for Board meetings five days in advance, except in the case of special meetings for which the time period may be shorter owing to the urgency of the matter to be considered. Xero's Company Secretary is responsible for supporting the effectiveness of the Board by ensuring that policies and procedures are followed and co-ordinating the completion and dispatch of the Board agenda and papers.

All Directors have access to executives, 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. Further, Directors have unrestricted access to company records and information.

The Board, the Board Committees and each Director have the right, subject to the approval of the Chairman, to seek independent professional advice at Xero'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 All Directors and employees are required to comply with Xero's Insider Trading Policy and Guidelines, in undertaking any trading in Xero shares. The table of Directors' shareholdings is included in the Disclosures section of this Annual Report.

Indemnities and insurance Deeds of Indemnity have been given to 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. Insurance is not provided for dishonest, fraudulent, malicious or wilful acts or omissions.

Board meetings The Board met formally eight times in the year ended 31 March 2011 and there were also separate meetings of the Board Committees. At each meeting the Board considers items of key financial and operational information as well as matters of strategic importance.

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

Directors who are not members of the Committees may attend the Committee meetings.

Board performance Board and Committee performance is subject to regular discussion at meetings of the Board and Committees.

Audit independence One of the main purposes of the Audit and Risk Management Committee is to ensure the quality and independence of the audit process. The Chairman of the Committee and General Manager Finance work with the external auditors to plan the audit approach. All aspects of the audit are reported back to the Committee and the auditors are given the opportunity at Committee meetings to meet in executive session with the Board.

Ethics The Board maintains high standards of ethical conduct and the Chief Executive is responsible for ensuring that high standards of conduct are maintained by all Xero staff, although no formal code of ethics is documented at this time.

DISCLOSURES

ENTRIES RECORDED IN THE INTERESTS REGISTER

The following are particulars of entries made in the Interests Register for the period 1 April 2010 – 31 March 2011.

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 2011.

Entity	*Relationship*
Sam Knowles	
Localist Limited	Chairman
Trustpower Limited	Director
Unlimited Realities Limited	Chairman
Government ICT Council	Chairman
Te Omanga Hospice	Trustee
Wellington Venues Limited	Director
Angel HQ Inc	Board member
United World College NZ	Trustee
Phil Norman	
KlickEx Corporation Limited	Became a director and shareholder
VoucherMob Limited	Became a director and shareholder
VIFX Systems	Became a director
VIFX General Partner Limited	Became a director
CloudFX Limited	Became a director
Graham Shaw	
Anaplan Inc	Became a shareholder
Craig Winkler	
BLD Group Pty Limited	Became a director
Anaplan Inc	Became an associated person of a shareholder
Pacific Fibre Limited	Became an associated person of a shareholder

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DISCLOSURES (CONTINUED)

Sam Morgan	
SMX Limited	Became an associated person of a shareholder
Anaplan Inc	Became an associated person of a shareholder
VendHQ	Became an associated person of a shareholder
Willis Bond Capital Partners Limited	Became an associated person of a shareholder

Share dealings of Directors Directors disclosed, pursuant to section 148 of the Companies Act 1993, the following acquisitions and disposals of relevant interest in Xero shares during the year ended 31 March 2011

	Date of acquisition/ disposal	Consideration per share	Number of shares acquired/ (disposed)
Rod Drury	22 July 2010	$1.45	(1,023,980)
Hamish Edwards	22 July 2010	$1.45	(288,913)
Sam Morgan	22 July 2010	$1.45	1,379,710

Shareholdings of Directors as at 31 March 2011

	Number of shares
Rod Drury	23,644,022
Hamish Edwards	6,671,087
Sam Knowles	205,555
Sam Morgan	4,290,427
Phil Norman	505,546
Graham Shaw	1,330,555
Craig Winkler	19,500,000

Unsecured loans were provided to Mr Norman and Mr Shaw during the year ended 31 March 2008 to purchase shares in Xero at $1.00 per share. Simple interest is repayable at a rate of 4% per annum, with the loans being repayable five years after the date of issue.

Remuneration of Directors Details of the total remuneration and the value of other benefits received by each Director of Xero during the financial year ended 31 March 2011 are as follows:

	Fees ($000s)	Salary ($000s)
Rod Drury*	–	256
Hamish Edwards*	–	169
Guy Haddleton**	30	
Sam Knowles***	12	
Sam Morgan	40	
Phil Norman	60	
Graham Shaw	40	
Craig Winkler	40	
	222	**425**

**Mr Drury and Mr Edwards are Executive Directors and receive remuneration from Xero in the form of salaries. They do not participate in the Xero Employee Restricted Share Plan.*

***Mr Haddleton ceased to be a Director on 17 December 2010.*

****Mr Knowles was appointed as a Director on 17 December 2010.*

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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 2011 are within the specified bands above $100,000. The remuneration figures shown in the table include all monetary payments actually paid during the course of the year ended 31 March 2011. It also includes the value of all restricted shares provided to individuals during the same period. The table does not include amounts paid post 31 March 2011 that related to the year ended 31 March 2011, such as the short-term incentive scheme bonus. The table below includes the remuneration of Mr Drury and Mr Edwards. No director of a subsidiary receives or retains any remuneration or other benefits from Xero for acting as such.

	Number of employees	Number of employees acting as directors of subsidiaries
$100,000 – 109,999	9	
$110,000 – 119,999	4	
$120,000 – 129,999	2	
$130,000 – 139,999	5	
$140,000 – 149,999	5	
$150,000 – 159,999	1	
$160,000 – 169,999	1	
$170,000 – 179,999	2	
$220,000 – 229,000	1	
$230,000 – 239,999	2	
$240,000 – 249,999	1	
$250,000 – 259,999		1
$270,000 – 279,999	1	
$330,000 – 339,999	1	
$340,000 – 349,000		1
	35	2

Analysis of shareholding as at 27 May 2011

	Number of holders	Number of shares	% of issued capital
1 – 1,000	514	341,481	0.38
1,001 – 5,000	859	2,459,203	2.70
5,001 – 10,000	444	3,251,991	3.57
10,001 – 100,000	497	10,619,524	11.67
100,001 and over	43	74,340,082	81.68
Total	**2,357**	**91,012,281**	**100.00**

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DISCLOSURES (CONTINUED)

Twenty largest shareholders as at 27 May 2011

Shareholder rank and name	Holding	Percentage of total shares on issue
1. Anna Stuck & Kenneth Drury (Rod Drury)	23,644,022	25.98
2. Givia Pty Limited (Craig Winkler)	19,500,000	21.43
3. Hamish Edwards & Tineke Edwards & Andrew Finch (Hamish Edwards)	6,671,087	7.33
4. Jasmine Investment Holdings Limited (Sam Morgan)	4,290,427	4.71
5. Valar Ventures LP	2,681,325	2.95
6. Bank of New Zealand	2,177,778	2.39
7. Anna Grigg & Alastair Grigg & Claymore Trustees Limited (Alastair Grigg)	1,533,594	1.69
8. Nicola Wilson & David Wilson & Christoper Ritchie	1,503,488	1.65
9. Graham Shaw & Delwyn Shaw	1,330,555	1.46
10. FNZ Custodians Limited	1,292,961	1.42
11. W5 Limited	995,561	1.09
12. Xero Limited (Employee Restricted Share Plan)	759,004	0.83
13. Craig Walker & Catherine Walker	715,757	0.79
14. New Zealand Central Securities Depository Limited	571,921	0.63
15. Andrew Finch & Raymond Bishop & Elaine Bishop	525,000	0.58
16. Philip Norman	505,546	0.56
17. Fletcher Brown & Karen Harness	464,000	0.51
18. ASB Nominees Limited	409,886	0.45
19. Philip Fierlinger & Hadley Fierlinger & Murray Harden	377,000	0.41
20. Binalong Rural Pty Limited	333,333	0.37

Substantial Security Holders According to notices given under the Securities Markets Act 1988 the following persons were Substantial Security Holders in Xero Limited as at 27 May 2011 in respect of the number of voting securities set opposite their names:

1. Anna Stuck & Kenneth Drury (Rod Drury)	23,644,022
2. Givia Pty Limited (Craig Winkler)	19,500,000
3. Hamish Edwards & Tineke Edwards & Andrew Finch (Hamish Edwards)	6,671,087

The total number of issued voting securities of Xero Limited as at 27 May 2011 was 91,012,281.

NZX Waivers Xero Limited has had no NZX waivers granted or published by NZX within or relied upon it in the 12 months immediately preceding 27 May 2011.

Subsidiary Company Directors The following people held office as Directors of subsidiary companies as at 31 March 2011:
Xero (UK) Limited – Rod Drury, Gary Turner
Xero Pty Limited – Rod Drury, Chris Ridd (appointed), Karen Gambles (resigned)
Xero Inc – Rod Drury
Xero Trustee Limited – Rod Drury, Graham Shaw

Annual Meeting Xero's Annual Meeting of shareholders will be held at the NZ Academy of Fine Arts, 1 Queens Wharf, Wellington on Thursday 21 July 2011 at 4pm. A notice of Annual Meeting and Proxy Form has been circulated to shareholders.

REGISTERED OFFICE:

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WEBSITE:

WWW.XERO.COM

DIRECTORS:

ROD DRURY
CHIEF EXECUTIVE, CO-FOUNDER

HAMISH EDWARDS
CO-FOUNDER

SAM KNOWLES

SAM MORGAN

PHIL NORMAN
CHAIRMAN

GRAHAM SHAW

CRAIG WINKLER

MANAGEMENT:

ROD DRURY
CHIEF EXECUTIVE, CO-FOUNDER

HAMISH EDWARDS
CO-FOUNDER

ALASTAIR GRIGG
CHIEF OPERATING OFFICER

PAULA JACKSON
GENERAL MANAGER MARKETING

PAUL WILLIAMS
GENERAL MANAGER FINANCE

LEANNE GRAHAM
COUNTRY MANAGER – NEW ZEALAND

CHRIS RIDD
MANAGING DIRECTOR – AUSTRALIA

GARY TURNER
MANAGING DIRECTOR – UNITED KINGDOM

AUDITORS:

PRICEWATERHOUSECOOPERS

LEGAL ADVISORS:

BELL GULLY

COMPANY SECRETARY:

LINDA COX
CORPORATE NAVIGATOR LIMITED

BANKERS:

ASB BANK LIMITED
BANK OF NEW ZEALAND LIMITED
HSBC LIMITED
NATIONAL AUSTRALIA BANK LIMITED

SHARE REGISTRAR:

LINK MARKET SERVICES LIMITED
LEVEL 16, BROOKFIELDS HOUSE
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