MELBOURNE IT GROUP

Melbourne IT Group

Annual Report

2016

Our Locations

Sydney

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Melbourne VIC 3000

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Level 7, 100 Wickham Street
Fortitude Valley QLD 4006

T +61 7 3230 7201
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Annual General Meeting

The Annual General Meeting (AGM) will be held -

On Monday, 29 May 2017 at 11.00 am
At Executive Room II
The Westin Melbourne
205 Collins Street
Melbourne VIC 3000

All shareholders are invited to attend the AGM or to complete and return the proxy form that accompanies the Notice of Meeting.

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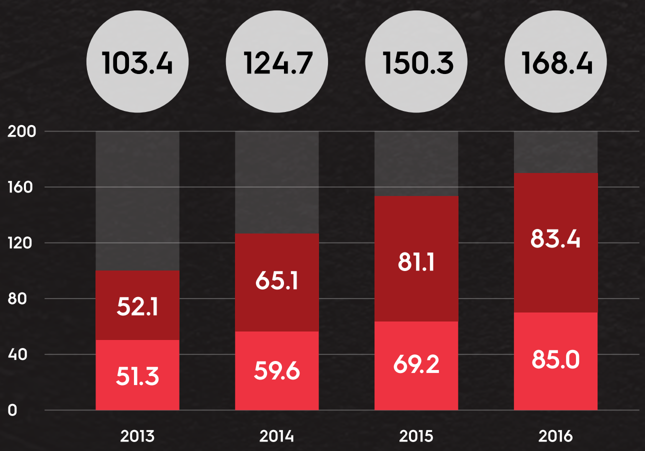
Our Purpose

We fuel our customers' success through the smart use of technology. We aspire to be Australia's most impactful digital technology partner.


LOGIN
PASS
OPTIMIZATION
IDEA
DEVELOP
COM

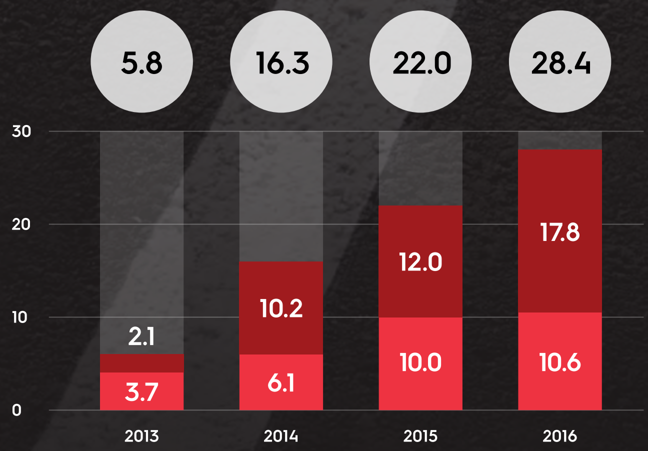
Financial Highlights of 2016

The future of Melbourne IT is all about growth. Our business has been completely transformed over the last three years, with our SMB business returning to growth after many years of continued decline and our Enterprise Services business tripling in size.



Revenue ($m)

Revenue has increased by 12% in 2016, and has increased by a compounded annual growth rate of 18% from 2013 to 2016.



Underlying EBITDA ($m)

Underlying EBITDA (Earnings Before Interest, Taxation, Depreciation and Amortisation) is Melbourne IT's preferred measure of profitability, and adjusts for one-off and non-recurring items and the pro forma impacts of acquisitions and divestments made in the financial period that may be included in the Reported EBITDA. Underlying EBITDA has increased by 29% in 2016, and has increased by a compounded annual growth rate of 70% from 2013 to 2016.

Acquisition of Data and Analytics Capability

In March 2016, we continued the expansion of the foundation digital technologies of our Enterprise Services business, adding data and analytics capability to our existing cloud, security, and mobile capabilities with the purchase of Infoready. We acquired 100% of this leading privately owned data and analytics business for $15.4 million. Infoready now operates as the data and analytics practice within Enterprise Services, with over 90 consultants across the East Coast of Australia.

100% Acquisition of Outware Systems

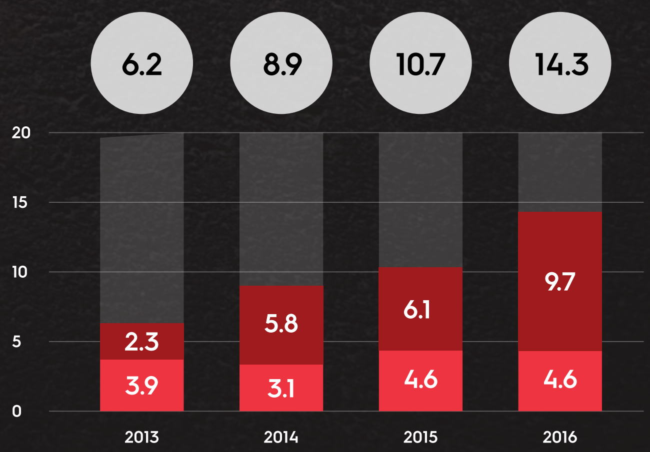
Following the the 50.2% acquisition of Outware in June 2015, we acquired a further 24.9% of Outware Mobile in August 2016, with the remaining 24.9% acquired in February 2017. This brought the Group's ownership of Outware Mobile to 100% allowing us to accelerate our plans to integrate our three Enterprise Services practices (Mobile, Data and Analytics, and Cloud and Security) to fully leverage our cross-practice capabilities while maintaining the strength and expertise of each practice as a standalone entity.

Sale of International Domain Name Registration business

In March 2016 we divested the International Domain Name Registration business for USD$6 million. The divestment of this non-strategic asset allowed for reallocation of capitol to our core strategy in the SMB business and reinvestment into growing our higher margin portfolio in digital solutions.

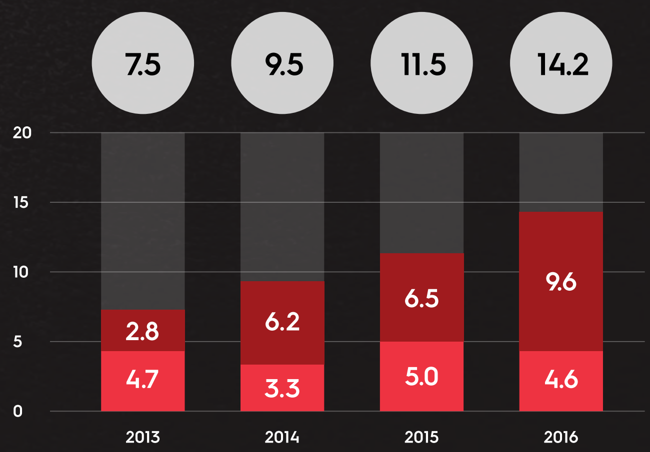
8.0 cents per share

The Group declared and paid an interim dividend of 2.0 cents per ordinary share, and declared a final dividend of 6.0 cents for 2016, an increase of 60.0% over the prior year. Both the interim and final dividend are fully franked (up from 80.0% franked in the prior year).



Underlying NPAT ($m)

Underlying NPAT (Net Profit after Tax) adjusts for one-off and non-recurring items and the pro forma impacts of acquisitions and divestments made in the financial period, to reflect the underlying performance of the Melbourne IT Group. A reconciliation between Underlying NPAT and Reported NPAT is presented on page 32 of this annual report. Underlying NPAT has increased by 34% in 2016, and has increased by a compounded annual growth rate of 32% from 2013 to 2016.



Underlying EPS (cents)

Underlying EPS (Earnings per Share) presents earnings per share after adjusting for one-off and non-recurring items and the pro forma impact of acquisitions and divestments made in the financial period. Underlying EPS has increased by 23% in 2016, and has increased by a compounded annual growth rate of 24% from 2013 to 2016.

Chairperson's Review

2016 was a huge year for Melbourne IT. Under CEO Martin Mercer's leadership, the turnaround of the business is complete, and both our Enterprise Services (ES) and Small and Medium Business (SMB) divisions exited 2016 growing at the top and bottom lines.

Transformation Complete

We have achieved the three main priorities that underpinned our turnaround.

Our SMB business, now under SMB Managing Director Emma Hunt's leadership, has returned to growth and we are ahead of schedule in realising the synergy savings expected from our acquisitions of Netregistry (February 2014) and Uber Global (April 2015).

Our Enterprise Services (ES) business, under the leadership of Peter Wright, has tripled in size over the last three years. We have 40% of the ASX Top 20 as customers and, with the acquisition of Infoready in March 2016, we have achieved our objective of assembling a broader portfolio of digital capabilities to help organisations become more competitive and more customer-centric.

Our future across the group is all about growth.

Delivering Shareholder Value

Melbourne IT has an ongoing commitment to creating value for its shareholders. We are pleased to deliver another solid result for shareholders, growing revenue and underlying EBITDA, adding new customers, and providing consistent shareholder returns. Over the last three years the Group has delivered strong growth, with revenue growing at a compounded annual growth rate (CAGR) of 18%, increasing from $103.4m in 2013 to $168.4m in 2016, with underlying EBITDA growing at a CAGR of 70% to $28.4m, and underlying EPS growing at a CAGR of 24% to 14.2 cents. Our consistent execution against a clearly defined strategy is driving strong growth in the business.

In both the SMB and ES divisions, we have diversified revenue streams to minimise overall business risk. Revenue quality, in the form of recurring annuity income and repeatable project revenue, has been maintained throughout our transition to a solutions business.

Considering the pleasing financial result for 2016, the Board of Melbourne IT has supported a 60% increase in our dividend to 8.0 cents per share (now fully franked).

Thanks

2017 marks the start of a new era for Melbourne IT. It is therefore an opportune time for me to hand over my leadership of the Melbourne IT Board to new Chairperson Gail Pemberton. Gail has been a member of the Board since May 2016 and brings with her a wealth of experience from the technology and financial services sectors. I am confident that Gail will expertly guide the business through this new chapter.

I joined the Melbourne IT Board in 2003, and was appointed Chairman in 2009. During this time I have witnessed its dramatic transformation firsthand. The business today is unrecognisable from the Melbourne IT of 13 years ago and I am looking forward to seeing the great things that it will accomplish in the future.

The transformation of our business could not have happened without the significant contribution and dedication of our people. I would like to thank all the individuals at all levels of our business who have embodied our values and worked tirelessly to improve our customers' experiences with us and to help us achieve our excellent financial results. I want to particularly express my sincere thanks to Martin and his Leadership Team for their superb job leading the business through this transformation.

Simon Jones
Chairperson (2016)

Looking Ahead

The year ahead will see a continued focus on delivering growth. We will be working on our employee value proposition and our remuneration and incentive schemes to make Melbourne IT an employer of choice and a great place to work for top technology talent. Aligned with this, we will also define a cohesive brand strategy that accurately reflects the transformation of the business.

We are part way through a Board refresh program that commenced 12 months ago under Simon, the former Chairman, with the aim of bringing in the right skills to support management for the next chapter of the company's growth. We have almost completed a process to recruit a director with skills relevant to our rapidly-growing Enterprise Services division. We hope to announce that appointment in the near term.

I would like to take this opportunity to thank Simon Jones for his dedication, focus, and hard work over the last decade, as he shepherded the company through its turnaround. His contribution will be sorely missed.

Inspired by the company's transformation, I joined the Melbourne IT Board to continue my passion of supporting Australian businesses who have innovation and technology as part of their core value proposition and an inclusive and collaborative culture. I am looking forward to working with Martin and his Leadership Team on the next stage of our growth.

Gail Pemberton
Chairperson (2017)

CEO's Report

In 2016 we completed the programme we embarked on three years ago to turn around the performance of our operating businesses and to restore the financial foundations of Melbourne IT. This is reflected in our 2016 results and in the performance over the past three years.

Martin Mercer
Managing Director and CEO

In 2016 we delivered strong growth in revenue (12%), EBITDA (71%) and NPAT (91%). Importantly, the growth in underlying EBITDA (29%) and EPS (23%) was also strong. The performance over the three years of our turnaround has been stronger still; revenue has grown at an annual compounding rate of 69%, underlying EBITDA at 70% pa, and underlying NPAT at 32% pa.

We enter 2017 with our Enterprise Services (ES) division enjoying strong organic growth and our Small and Medium Business (SMB) division returning to organic growth after a protracted decline.

While we printed a very pleasing set of results, a more substantial achievement was the progress that has been made in building a platform for sustainable growth.

The Melbourne IT of today is almost unrecognisable from the Melbourne IT of three years ago.

In 2013 Melbourne IT sold its Digital Brand Services division and a smaller business known as For the Record. After this, Melbourne IT had two remaining business divisions; Small and Medium Business (SMB) and Enterprise Services (ES). SMB sold domain names and hosting services to small businesses, and ES sold hosting solutions (both dedicated hosting and cloud managed services) to large companies and government agencies.

In 2013, the SMB division declined by 7% in revenue terms and 35% in EBITDA terms, and the ES division declined by 6% in revenue terms and 42% in EBITDA terms. In 2014 we set about rebuilding these businesses and repairing the financial foundations of Melbourne IT.

The turnaround of Melbourne IT is complete, and has entailed a top to bottom re-imagining of every aspect of the business. ES, once the poor cousin to SMB, has been transformed into a rapidly growing provider of complete digital solutions for large companies and government agencies. In the three years since 2013 it has tripled in size and exits 2016 growing at approximately 20% pa. It is now the leading provider of managed digital solutions for large companies and government departments and is uniquely positioned to ride on the tailwinds of growth in digital services.

And while SMB still has one foot in its legacy domains and hosting business, its future is in managed digital marketing solutions for small businesses. Revenues from these new services already account for more than 20% of direct revenue and are growing at almost 60% per annum. In a major milestone, SMB returns to organic growth in 2016.

If the last three years have been characterised by the hard and painstaking work of rebuilding and transformation, the future will be characterised by innovation and accelerating organic growth.

In addition to the improving financial and operational performance of our business we continued to make progress on building a dynamic organisation populated by committed people with a passion for delivering exceptional outcomes for customers and shareholders.

Our priorities for this year are subtly different to past years and reflect a changing emphasis as we shift from rebuilding to accelerating growth. In 2017 we must;

1. attract, develop, and retain talented people and create an even more vibrant workplace
2. continually iterate and improve customer experience at every opportunity because this will set us apart from our competition and is a great rallying cry for our people
3. capitalise on the successful move into managed marketing solutions for small businesses & transform Melbourne IT into the leading provider of managed marketing solutions for small to medium businesses
4. capitalise on the transformation of our ES division into the leading provider of managed digital solutions for large enterprise and government customers

> "This sustained focus on the financial, operational, and cultural health of our company is transforming the business and delivering significant value to shareholders."

2017 Priorities

1 Attract, Develop, and Retain Talented People

The growth in both ES and SMB is being driven by the growth in our solutions offerings. These solutions services are developed, delivered and supported by people and as this part of our business grows the number of people working in Melbourne IT will grow commensurately. Our ability to attract, develop and retain an increasing number of talented people is critical to the successful execution of our strategy.

At Melbourne IT a focus on the development of our people and the creation of meaningful work is a priority for us. We believe that the happiness of our people and the returns to our shareholders are both important and inextricably linked. We need to attract, develop and retain great talent in the business resulting in an engaged, motivated and high performing workforce.

In 2016 we continued to invest in leadership development and specific skills training. We believe that leadership at every level is essential to performance and engagement. As we shift from a platform business to a business that scales with people the emphasis on culture and the creation of meaningful work becomes paramount.

2 Iterate and Improve Customer Experience

We measure customer sentiment using the 'Net Promoter Score', an established model for measuring customer loyalty.

For the past couple of years the measurement of NPS has been confined to our SMB division and to a subset of customer touch points. In the second half of 2016 we implemented holistic NPS measurement across both SMB and ES.

We enjoyed steady improvement over the second half of the year but now that we have a consistent approach across both of our divisions this will become a key metric. We anticipate continuing improvement as we transform ourselves into a true customer company.

This will provide sustainable differentiation, fuel growth, and catalyse change across our business. Viewed this way, a focus on customer excellence is a critical tool in galvanising the engagement of our people and delivering shareholder return.

3 Capitalise on Solutions Growth in SMB

A key focus in our SMB division over the past couple of years has been the integration of acquired businesses and the realisation of synergy savings. This process is now largely complete and $8.5M of the anticipated $10M of annualised savings have been realised. Over this time we have also succeeded in stabilising the performance in the legacy business (ie domains and hosting).

Two years ago we launched two new products targeted at a clear opportunity in "done for me" managed digital marketing for SMBs. Later we added additional products to our suite of managed marketing solutions. Throughout 2015 and 2016 we have enjoyed consistent growth in sales of these solutions products. In 2016 revenue from these new solutions products accounted for 20% of direct revenues and grew at almost 60% year-on-year.

Given the progress we have made in 2016, we are forecasting top and bottom line growth for our SMB division in 2017. This is a major milestone in the turnaround of this division.

4 Capitalise on the Transformation of Enterprise Services

The transformation of our Enterprise Services (ES) division from a dedicated hosting business to a provider of managed digital solutions for large enterprise and government customers is essentially complete.

The acquisition in 2015 of Outware Systems, the leading developer of enterprise grade mobile applications, was followed in 2016 by the acquisition of Infoready, a leading provider of data and analytics solutions for large enterprise and government customers. As result, we now have established expertise in the foundation digital technologies of cloud, security, data and analytics, and mobile.

These technologies form the building blocks of comprehensive digital solutions and are the bedrock of our future growth. In 2016 revenue in ES grew 73% and revenue from solutions services comprised 97% of total revenue.

The successful transition of ES from a mature infrastructure business to an expanding digital services business is essentially complete and we expect strong growth in this division.

Looking Ahead

The work of rebuilding and strengthening our business is essentially complete. We now enter a new chapter in the Melbourne IT story, a chapter characterised by accelerating organic growth.

The accelerating financial performance in SMB and ES is like rocket fuel for the confidence of our people. It makes sense of a tumultuous few years and restores certainty and optimism. Over 2017 we will redouble our efforts in building a culture of excellence. We have a very ambitious target for measured staff engagement in 2017 and we will continue with our focus on building capability and investing in the development of our people.

This sustained focus on the financial, operational, and cultural health of our company is transforming the business and delivering significant value to shareholders.

SMB Solutions

In 2016, SMB returned to growth, with revenue increasing 4% year-on-year. We acquired more than 50,000 new customers and our managed marketing services strategy is rapidly accelerating, with more than 20% of SMB revenue coming from this portfolio and growing at 56% year-on-year.

The Small Business division (SMB) enables Australian small businesses with online marketing solutions, providing them with the tools to grow and thrive online. We have over 450,000 direct customers and provide services to over 700,000 Australian businesses to help them grow online. Our services include domain names and hosting services, as well as managed marketing solutions helping small businesses create an online presence, and then grow and thrive in this increasingly complex environment.

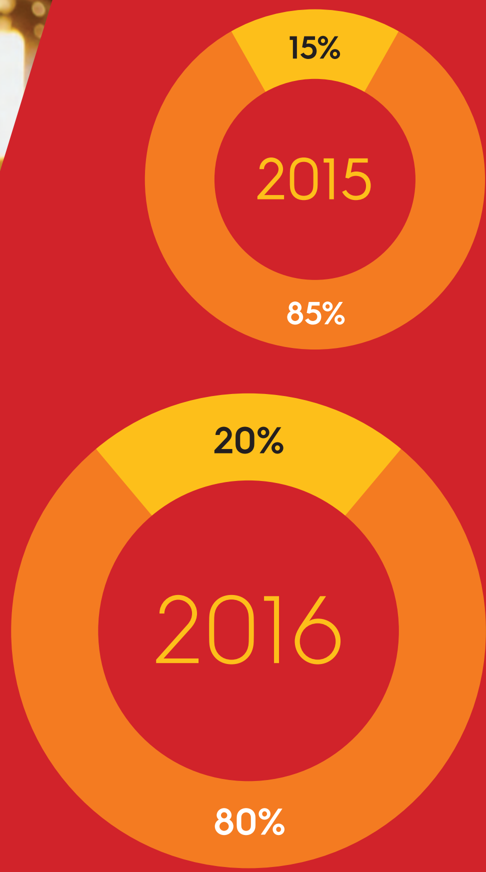
Melbourne IT is the leading Australian domains and hosting business with over 40% share of volume and 50% revenue market share. But the domains and hosting market has been commoditised in recent years, margins have been compressed and growth is slowing. This legacy business is unlikely to be a long-term source of growth and we are re-investing the cash from this business in a wide open opportunity in managed marketing solutions across website design and management, and search engine and social media marketing services.

2016 Highlights

Our core strategy in 2016 focused on the twin goals of strengthening our legacy domains and hosting business by focusing on automation and reducing the cost to serve, while leveraging this large existing customer base to rapidly accelerate the attachment of online marketing solutions.

SMB returns to growth

It was a watershed year for SMB, with the business returning to growth. Revenue grew 4% year-on-year, once normalised for the divestment of the International Domain Name business and the Uber Global acquisition, and the SMB business acquired more than 50,000 new customers in 2016. This is the first period of organic growth in many years and demonstrates the strong momentum in the SMB business as we nurture and protect the legacy domains and hosting business, while accelerating



SMB

Revenue split by numbers

Solutions Components

Segment result

(continuing operations)

Revenue

↑4% change

$88.8m FY 15

$92.5m FY 16

EBITDA Contribution

↑11% change

$14.0m FY 15

$15.6m FY 16

growth of the managed marketing services portfolio. This growth was largely due to increasing numbers of customers in the direct business using marketing solutions, and strong renewal rates in the legacy domains and hosting revenue. We also saw strong performance from the indirect business through activities to correct the declining trend seen over the last few years and to close flat year-on-year.

A key performance driver in 2016 was the divestment of the International Domain Name Registration business which allowed for reallocation of focus and reinvestment into growing the core higher margin portfolio.

Online marketing specialist capability

Importantly, in 2016 we saw the rapid acceleration of our managed marketing services strategy with more than 20% of SMB direct revenue coming from this portfolio, and growing at 56% year-on-year. Our hypothesis has been that there is a large market opportunity to support small businesses with their online presence – developing a website and supporting their online marketing activities. The results in 2016 have proven this to be true, and in delivering these services to small businesses we have significantly increased Average Revenue Per User (ARPU) at the same time. Growing ARPU will be central to our plan in 2017 as we support even more small businesses with multiple managed marketing solutions. Our customers are looking for a trusted partner to help them choose the best way to get found online, whether via a website or through social media channels, and use this online presence to attract and retain customers.

2017 Outlook

Our priority in 2017 will be to take these learnings from 2016, and accelerate our managed marketing solutions strategy.

Our strategy is to support small businesses with their online journey and to help them succeed online. They will start the journey with us, registering their domain name as a first step to establishing their online presence. We will then build their website and deliver their online marketing campaigns to drive

traffic to their website, generate new customer opportunities, and ultimately help them grow their business. Through this journey, we will take a customer who used to spend $100pa with us and turn them into a customer who spends $6,000pa with us.

Accelerating our marketing services strategy

Investing in this online marketing specialist capability across our sales teams is a priority, with a focus on developing subject matter experts (eg. Social media marketing experts) in specialist teams. Alongside this, we are introducing dedicated SMB Account Managers who will deliver exceptional customer experiences while understanding where our customers are on their digital journey, identifying their business needs and opportunities to help them be successful.

Deep understanding of our customers

Key to success in 2017 will be developing an insight-rich view of our customer base so that we will be able to engage and support them in a more personalised way. Understanding which industries our customers are working in, how large their businesses are, and what their priorities are will help us make sure we are talking to them about solutions and industry trends that are relevant to them. This will ensure that when they are thinking about the next step in their online journey, Melbourne IT is the first place they start.

A key enabler of this will be the consolidation of our large customer base onto a single platform, with the completion of the Integration programme. This will allow us to leverage the rich customer information we have and use it to better support our customers.

Product innovation

Product innovation will also be a focus, delivering inventive, easy-to-use solutions that simplify the process of establishing, managing and growing an online presence. We will continue to enhance and evolve our offering based on understanding deeply the needs of our customers.

By focusing on accelerating the growth of our Marketing Solutions business while nurturing our large legacy customer base, the SMB division is well positioned to accelerate growth in 2017.

"Our strategy is to support small and medium businesses with their online journey and to help them succeed online."

ES

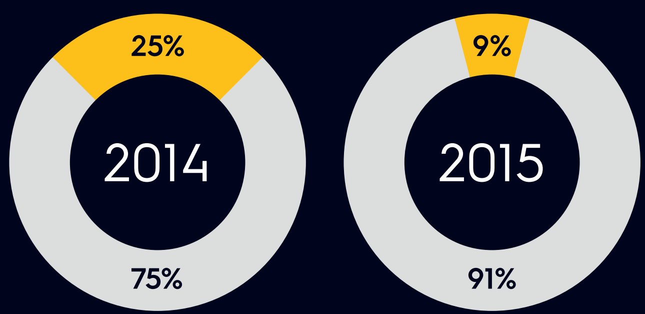
Enterprise Services

In 2016, Enterprise Services grew 73% to $70.4m while EBITDA grew 87% to $14.6m as enterprise and government organisations continue to invest in digital technologies to fuel competitiveness.

ES

Revenue split by numbers

Solutions Infrastructure



The evolution of digital technologies has substantially reduced the cost and time of building and managing technology-based solutions, enabling enterprises to keep pace with their business needs. People in enterprises are liberated to focus on creating new products, services and other business improvements. They partner with technology experts to rapidly bring their ideas to life.

Enterprise Services is known in the market as partnering with our customers to help them become more competitive and more customer centric. We have expertise in customer-focused design, software engineering, data analysis and management of flexible digital solutions across foundational technologies Mobile, Data and Analytics, Cloud and Security. This expertise, and our ability to combine these foundational technologies into solutions, sets us apart as the most impactful digital technology partner for the enterprise market.

2016 Highlights

Enterprise Services' growth is underpinned by our ability to help organisations increase their rates of innovation, better understand their customers, and improve their overall competitiveness.

Strong revenue and customer growth

In 2016 revenue grew 73% to $70.4m while EBITDA grew 87% to $14.6m as enterprise and government organisations continue to invest in digital technologies to fuel competitiveness.

Recurring revenues continue to grow as a percentage of overall revenue, up 3% over 2016 to 90% of total revenue. Managed Services and repeatable project revenues both grew as customer relationships become more strategic.

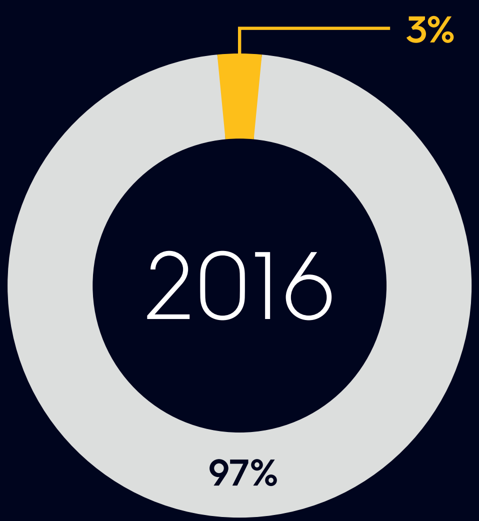
New customer acquisition is healthy. This is demonstrated by our new partnerships with organisations such as Crown, Tabcorp, The Link Group, Qantas, Jetstar, Officeworks & Peoplecare, while Queensland Education, a long term Enterprise services customer, has re-signed with us for a new three-year term.

Permanent staff numbers have increased from 191 to 286 with staff located in Queensland, NSW, ACT and Victoria. Enterprise Services is committed to investing in and retaining the best talent in the industry across the foundation disciplines of mobile, analytics, cloud and security as well as combining these capabilities to innovate across the latest digital technologies. With a focus on helping customers deliver new products and services to market, the Enterprise Services employee value proposition is based on innovation, the ability to work on high profile, challenging projects, work with new digital technologies and collaborate with other high achievers. Our culture and employee value proposition differentiates Enterprise Services in the evolving digital technologies market.

Completing our range of specialist capabilities

Enterprise Services has pursued a strategy of building deep competencies across the foundation digital technologies of mobile; data and analytics; and cloud and security. In line with this strategy, in 2016 we acquired leading data and analytics firm, Infoready, to complete this range of capabilities.

This approach provides us with the skills and competencies to help leading organisations extract maximum value from their use of digital technologies. It also enables us to help them take advantage of the latest generation of digital technologies such as chatbots, virtual reality, and advanced machine-to-machine learning, which all use a combination of the foundational digital technology skills.



Revenue

↑73% change

$40.7m FY 15

$70.4m FY 16

EBITDA Contribution

↑87% change

$7.6m FY 15

$14.6m FY 16

We have demonstrated our ability to expand services across practices as customers continue to seek more expansive and sophisticated solutions to meet their business needs. 10% of our customers now take services from more than one practice.

Industry recognition

Enterprise Services operates primarily at the value end of the market. Deep expertise, demonstrated ability to innovate, and a focus on people underpins our performance. In 2016 we achieved AWS Premier Partner recertification, the AWS Marketing Competency, and the new AWS Public Sector Competency.

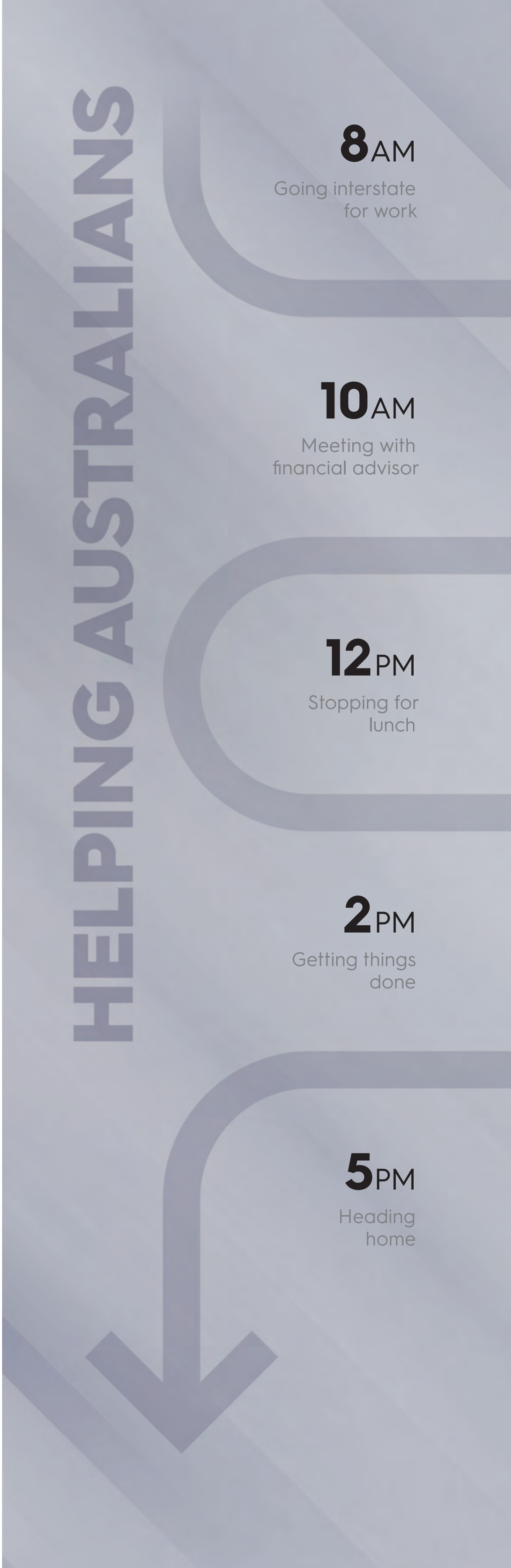
Other awards recognising our skills and achievements include IBM Commercial Sector Partner of the Year and Design100 Best App Design Studio for the 4th consecutive year, while a number of our mobile solutions also received recognition, including Opal Travel winning gold at the Sydney Design Awards and the Gov Design Awards.

2017 Outlook

Australian organisations continue to adopt digital technologies at pace to help drive competitive advantage.

Enterprise Services is well placed to benefit from this demand and has built an enviable portfolio of digital solutions. We partner with corporates to improve the lives of everyday Australians by helping them to get things done, be more productive, learn, grow, thrive and be entertained. We are uniquely positioned to help organisations become more competitive and more customer centric.

A track record in turning new ideas into effective products and services, deep expertise across foundation digital technologies and strong relationships with the Australian enterprise market will see Melbourne IT continue to grow strongly. We are optimistic about the outlook for 2017.



Book taxi to airport

CabFare

We built the CabFare mobile app which lets people automatically pay for the taxi ride and has additional safety features, for example giving the rider the taxi details and driver's number

Fly to Sydney

Jetstar

We are helping Jetstar improve their customer satisfaction scores by analysing and interpreting large amounts of customer feedback data through insightful data science

Check super balance

AustralianSuper

We manage and operate the platform which securely stores more than 2 million members' superannuation statements so they are easily and reliably accessible online

Check bank accounts

ANZ

We partner with ANZ on the Go Money app, used by more than 1.5 million Australians, which allows the user to do their banking securely from their mobile phone

Review transactions

Coles Financial Services

We built and continue to manage the performance of the Coles Mobile Wallet app which lets Coles Mastercard customers check balances and transactions easily and securely

Order pizza

Domino's

We manage the performance of Domino's online ordering platform, a high volume critical site, and the dissemination of those orders to thousands of stores world wide

Look up fire warnings

NSW Rural Fire Service

We created a fully scalable website solution that provides reliable fire updates and warnings for millions of Australians. We continue to manage this service ongoing

Answer mobile

Telstra

To improve the performance of the Telstra telephone network, we analyse performance data to determine the optimum size and location of network services

Plan trip to airport

Transport for NSW

We built the two Opal apps - one for customers to plan trips, check fares and recharge cards, and one for ticket inspectors to use to check validity of cards. We manage the performance ongoing

Check-in via app

Qantas

We partner with Qantas to improve the Qantas App, Qantas Entertainment and Qantas Loyalty apps. We also help improve the digital customer experience by analysing customer interactions

Read AFR on iPad

Fairfax Media

We partner with Fairfax Media on the Australian Financial Review app which gives consumers an intuitive mobile experience when consuming current digital content

Book a premium event

Foxtel

Foxtel's agile Cloud delivery model, managed by Melbourne IT, allows new services to be rapidly brought to market and improves Foxtel's competitiveness in video-on-demand market

OUR PEOPLE

2016 has been a year of significant growth & change for our people.

We are growing & expanding

Through both organic and inorganic growth over 2016, our total permanent employee base has grown to 560, with additional headcount of 230 when including professional contractors and offshore staff. This headcount growth has coincided with structural changes and headcount reductions both onshore and offshore as a result of integration, divestments, and productivity gains. This growth provides more opportunities for internal movements and promotions for our people, and allows room for the introduction of valuable new talent into our business.

In 2017 we will continue to invest in tools and initiatives to enable further growth. Recruitment is an important focus under a united group recruitment team. We are currently launching an enhanced recruitment system which will allow us to share and view candidate pools across the group, leverage networks, and more efficiently manage our process of on-boarding and engaging the right people. We will also be investing in careers fairs and internal graduate programmes so we can continue to build the next generation of specialist skills across our business.

"We are changing, bringing teams together and growing"

Bringing our teams together

Following these key acquisitions, we have been focusing on people integration activities to bring our new and existing teams and cultures together. Both the Outware and Infoready teams have co-located nationally (in Melbourne, Sydney, and Brisbane offices) with our Melbourne IT teams. Bringing these different businesses and cultures together creates greater opportunities for interaction, knowledge-sharing, and collaboration on go-to-market activities and customer engagement.

While our footprint in our Australian offices is growing, our teams based externally on client sites continue to be an important part of our growth and successful client partnership model. The leaders of these teams work hard to ensure offsite teams stay connected, engaged, and productive through initiatives like creating community hubs in key locations around client sites and leveraging virtual collaboration tools.

We have been exploring initiatives to provide opportunities for inter-office team building and interaction, for example running LAN parties for after-hours gaming across our locations.

Our structure has evolved

With growth comes complexity, and as such our business model and organisational design evolved significantly in 2016.

In August, we appointed Emma Hunt as Managing Director of our Small and Medium Business (SMB) division, and aligned key SMB functions underneath this role. Emma's appointment means that we now have dedicated leadership and a laser-like focus in both our SMB division and our Enterprise Services division as we set ourselves up for the next stage in our growth.

Key acquisitions in our Enterprise Services division – namely Outware Mobile in 2015 and Infoready in 2016 – have also resulted in structural realignments and team mergers that will enable us to fully leverage the expertise of our people across each of the practices.

With our growth expected to continue in 2017, our focus for the year ahead is on scalability. We will be continuing to amalgamate structures and eliminate duplicated processes and systems.

Cultivating culture

With all these businesses and cultures coming together, a key focus area for 2017 will be our brand identity, both internally as an employer and in the market for our customers. We will be conducting a comprehensive brand review aligned with the future direction of our business.

From a people perspective, defining and aligning our internal brand is critical to our future. We are thinking about our values, what it's like to work and grow in our business, and how we can further develop our employee value proposition: creating meaningful work for our people and making this a great place to work. We are excited about the future and how we position our values, cultural markers, and employee benefits and perks to reward and retain great people.

Our investment in and commitment to leadership development is ongoing. Leaders at all levels, from the executive team to people managers right across the group, have a stated commitment to personal development in this area. Our focus is on authenticity, self-awareness, and coaching capabilities, as well as core people management skills. These capabilities are

The Executive Team

Previous CFO Peter Findlay left the business in January 2017. Stuart Bland was appointed CFO in March 2017.

Martin Mercer
Chief Executive Officer

Emma Hunt
Managing Director, Small & Medium Business

Peter Wright
Managing Director, Enterprise Services

Stuart Bland
Chief Financial Officer

Amy Rixon
Chief People Officer

Brett Fenton
Chief Technology Officer

fundamental in enabling sustainable growth in our business through engaging, developing, and growing all of our people. In 2017 we have arranged for a facilitator to be based on-site three days a week to provide one-on-one coaching to leaders, further embed our core leadership frameworks, and build skills through structured development labs.

Employee engagement remains an important focus for our business. We partner with an external agency to run a comprehensive culture and engagement survey annually which, in conjunction with quarterly pulse surveys and regular feedback sessions, helps us turn ideas into action plans that continue to drive improvements in employee engagement. As our business continues to change and grow, we need to keep engagement front and centre for our leadership.

A culture of innovation is critical to our success in the fast-paced technology industry. As such we continue to celebrate innovation and invest in training and skill development in this area. 2016 saw us hold our inaugural group-wide 'Hackathon', a truly unique, innovative, and culture-building initiative born out of Outware Mobile, where our people collaborate across locations on building innovative solutions to problems. We have dedicated innovation functions in both our ES and SMB divisions.

We recognise the importance of supporting our employees' health and wellbeing. 2016 saw us launch a new partnership with an Employee Assistance Program provider, giving employees free access to counselling, meditation sessions, and other wellbeing support services. In addition, we provide free gym memberships local to each of our offices and we have run a number of internal initiatives including healthy smoothie mornings and yoga classes.

Valuing diversity

We are proud of our diverse business, with over 50 nationalities and backgrounds represented across our teams. We continue to focus on improvements in building female diversity across the business and noted improvements in overall female representation, particularly at a leadership and board level. We have made efforts in setting up internal supporting and networking groups, as well as male champion of change initiatives. We have also reviewed our recruitment practices to attract and shortlist a greater number of female candidates in conjunction with thinking through our workplace flexibility and support.

Diversity continues to be in focus for the year ahead. We are kicking off with International Women's Day celebrations and broader initiatives around Women in Technology forums. As the year progresses we will continue to look for and seize other opportunities to celebrate the diversity of our people.

Our business has an exciting year ahead, one that builds on the foundational changes of 2016, continues to grow and develop our people, and lives up to our purpose: creating meaningful work for our people and fuelling the success of our customers through the smart use of technology.

BOARD OF DIRECTORS

Gail Pemberton

Chairperson (2017)

Ms Pemberton is a company director with more than 30 years of executive experience in the financial services industry. She held various senior roles as CEO and Managing Director for Australia and New Zealand, then Chief Operating Officer UK, at BNP Paribas Securities Services; Group CIO then Chief Operating Officer of the Financial Services Group at Macquarie Bank.

Ms Pemberton is currently the Chair of OneVue Holdings Ltd, non-executive director of Paypal Australia and Eclipx Ltd. She also held directorships at QIC Limited, SIRCA, RoZetta Technology and UXC. She has a Master of Arts from the University of Technology Sydney, is a fellow of the Australian Institute of Company Directors and a member of Chief Executive Women.

Ms Pemberton joined the Board on 27 May 2016 and was appointed Chair on 1 February 2017. She is a member of the Audit & Risk Management Committee and the Human Resources, Remuneration & Nomination Committee.

"We are focused on attracting and retaining top technology talent, delivering strong growth for our shareholders, and fueling the success of our customers."

Martin Mercer

Managing Director & CEO

Mr Mercer was appointed as Managing Director and Chief Executive Officer on 7 April 2014. Prior to joining Melbourne IT, he was Managing Director, Strategy and Fixed at Optus following four successful years as CEO of vividwireless, and ten years in a number of significant leadership positions at Telstra. Mr Mercer has an impressive resume in strategy, sales, marketing and product development and general management and brings with him a reputation for excellence in both strategy and execution.

Mr Mercer has a BA (Hons) and an LLB from the University of Sydney, and a graduate diploma in Finance from the Securities Institute of Australia. He studied economics and finance at the Woodrow Wilson School of Public and International Affairs, Princeton University and is also a former Harkness Fellow.

Simon Jones

Chairperson (2016)

Mr Jones is a Chartered Accountant and a director of Canterbury Partners Pty Ltd, a corporate advisory business. He has extensive experience in investment advisory, valuations, mergers and acquisitions, public offerings, audit and venture capital.

Mr Jones is Chairman of Computershare Limited, the Advisory Board of MAB Limited and the Advisory Board of Trawalla Group. He is a former Managing Director of N.M. Rothschild and Sons (Australia), Melbourne and also former Head of Audit and Business Advisory (Australia & New Zealand) and Corporate Finance (Melbourne) of Arthur Andersen.

Mr Jones joined the Board on 12 March 2003. He was Chairman of the Board for over 7 years from 1 November 2009 until 1st February 2017. He is a member of the Audit & Risk Management Committee and, until recently, was also a member of the Human Resources, Remuneration & Nomination Committee.

Naseema Sparks AM

Non-Executive Director

Ms Sparks is an experienced top-line growth director with expertise in a range of industries. Her expertise includes corporate strategy, online commerce, retail, financial services, media, branding and marketing, and digital technology platforms. She was former Managing Director and Global Partner of M&C Saatchi Ltd. She holds an MBA from Melbourne Business School and is a Fellow of the Australian Institute of Company Directors.

She is a director of several Australian publicly listed, private and not-for-profit entities, including PMP Ltd, Australian Vintage Ltd and AIG Australia. She also serves on boards of emerging technology companies at scale-up stage. She was former Deputy Chairman of Racing NSW and non-executive director of Blackmores Ltd and Grays e-Commerce Group Ltd.

Ms Sparks was appointed to the Board on 19 April 2012. She is Chairperson of the Human Resources, Remuneration & Nomination Committee.

John Armstrong

Non-Executive Director

Mr Armstrong is an experienced company director and financial professional. He was the former CFO of SEEK Limited, a role he held for over 12 years, and director of SEEK's business in China, Zhaopin Ltd, and SEEK Asia. He also held management roles at Carlton & United Breweries and commenced his career at Ernst & Young. He is currently a director and member of the Audit & Risk Committee of Blackmores Ltd and was also a director and Chair of the Audit & Risk Committee of iProperty Ltd.

Mr Armstrong holds a Bachelor of Business (Accounting) and is a member of the Australian Institute of Company Directors.

Mr Armstrong was appointed to the Board on 23 February 2016. He was a member of the Audit & Risk Management Committee, and appointed Chairman of the Committee on 27 May 2016.

Larry Bloch

Non-Executive Director

Mr Bloch has been a serial entrepreneur, pioneer and leader in the online business services industry for 20 years. He was the founder and former MD of NetBenefit (UK) in 1994 which rapidly became the largest domain and hosting provider in Europe. He also founded Virtual Internet (France) in 1996. After re-locating to Australia in 1997, he co-founded Netregistry Group and was its major shareholder, CEO and Chairman for 17 years, before selling it to Melbourne IT in 2014.

Mr Bloch holds a Bachelor of Science and Post Graduate Honours degrees in Pure Mathematics and Computer Science from the University of Cape Town.

Mr Bloch was appointed to the Board on 3 April 2014. He is a member of the Human Resources, Remuneration & Nomination Committee and Audit & Risk Management Committee.

Tom Kiing

Non-Executive Director

Mr Kiing is a director of Bridge Capital Pty Ltd, an Australian technology investment firm that manages a portfolio of investments in the IT sector. He currently sits on the Boards of: Primary Opinion Ltd, an ASX listed food business; and The Atomic Group, an integrated retail sports and health company in Australia.

Mr Kiing has extensive experience in mergers and acquisitions, capital markets and corporate finance. He travels extensively through the ASEAN region to promote a wide range of Australian investment opportunities to Asian institutions and private investors.

Mr Kiing was appointed to the Board on 19 December 2002. He is a member of the Human Resources, Remuneration & Nomination Committee.

Rob Stewart AM

Non-Executive Director

Mr Stewart is a company director and management consultant with extensive experience from leading companies across a variety of industries. He held directorships in various publicly listed companies, including Mitchell Communications Group Ltd, Metabolic Pharmaceuticals Ltd and Memtec Ltd, as well as a number of private commercial and not-for-profit entities, including the Baker IDI Heart and Diabetes Research Institute, where he was Chairman for six years. Currently, he is Chairman of C E Bartlett Pty Ltd, jobsjobsjobs Pty Ltd; and QSR International Pty Ltd.

He was a former National Managing Partner of Minter Ellison and held various management positions with Pacific Dunlop.

Mr Stewart joined the Board on 14 September 1999 and was Chairman until 31 October 2009. He was Chairman of the Audit & Risk Management Committee until his retirement from the Board on 27 May 2016.

Directors’ Report

Your directors submit their report for the year ended 31 December 2016.
Directors were in office for the entire period unless otherwise noted.

Directors
Ms Gail Pemberton (Appointed 27 May 2016) (Appointed Chair 1 February 2017)
Mr Simon Jones (Chairman to 1 February 2017)
Mr Tom Kiing
Ms Naseema Sparks
Mr Larry Bloch
Mr John Armstrong (Appointed 23 February 2016)
Mr Robert Stewart AM (Retired 27 May 2016)

Managing Director
Mr Martin Mercer

Company Secretary
Ms Edelvine Rigato

Details of directors' experience, expertise and directorships

Full details of the directors' experience, expertise and directorships can be found on the Melbourne IT website at www.melbourneit.info and the Annual Report.

Interests in the shares and performance rights of the company

As at the date of this report, the interests of the directors in the shares and performance rights of the company were:

	Ordinary shares	Performance rights[1] over ordinary shares
Ms Gail Pemberton	51,285	-
Mr Simon Jones	157,201	-
Mr Tom Kiing	5,721,488	-
Ms Naseema Sparks	6,612	-
Mr Larry Bloch	9,458,363	-
Mr John Armstrong	-	-
Mr Martin Mercer	-	801,081

(1) Performance rights are zero-priced options over the ordinary shares of Melbourne IT Limited.

Principal activities

The principal activities of the Group during the year by operating segment are described as follows:

Enterprise Services (ES)

Enterprise Services provides services including cloud, mobile application development, data and analytics to Australian enterprise and government organisations.

Directors' Report

SMB Solutions

SMB Solutions provides domain name registrations and renewals, website and email hosting, website development, search engine optimisation and analysis for businesses in Australia and New Zealand.

Review and results of operations

Earnings per share

Total operations	2016 Cents	2015 Cents
Basic earnings per share	10.86	6.04
Diluted earnings per share	10.67	5.95

Dividends

During the year, a final dividend of 4.0 cents per share, amounting to $4,017,000 was paid on 29 April 2016 and an interim dividend of 2.0 cents per share, amounting to $2,015,000 was paid on 30 September 2016.

After 31 December 2016, a final dividend of 6.0 cents per share amounting to $6,052,000 was declared by the directors. The final dividend has not been recognised as a liability as at 31 December 2016.

Review of operations

Overview

The Group recorded a 12.1% increase in consolidated revenue during the year ended 31 December 2016, from $150,256,000 to $168,436,000. This was primarily due to the full year contribution of Uber Global and Outware Systems that joined the Group on 30 April 2015 and 16 June 2015 respectively, and the newly acquired entity, InfoReady Pty Ltd, acquired in March 2016. The increase in revenue was partially offset by the divestment of the International Domain Name Registration (IDNR) business on 31 March 2016.

The Group achieved earnings before interest, tax, depreciation and amortisation (EBITDA) of $28,206,000 (2015: $16,510,000), an increase of 70.8% from the previous year. Consolidated net profit after tax was $12,708,000 (2015: $6,728,000), up 88.9% from the previous year. Underlying earnings per share has also increased to 14.22 cents per share, up 23.1% from the previous year.

The integration of Netregistry and Uber is forecast to deliver $10,000,000 of annualised synergies savings by the end of 2017, with annualised synergy savings of $8,500,000 already achieved by the end of 2016.

The Group continued to generate strong operating cash flows, with $14,302,000 of cash flows from operating activities achieved in 2016. The cash balance of $16,426,000m as at 31 December 2016 demonstrates the strength of our balance sheet.

The Group believes that the inclusion of non-IFRS, unaudited information in the following tables are relevant to the user's understanding of its results as it provides a better measure of underlying operating performance.

Directors' Report

Summarised operating results are as follows:

	2016 $'000	2015 $'000
Revenue		
Registration revenue	44,916	55,932
Solutions, hosting & services	123,253	94,041
Other revenue	-	21
Total revenue excluding interest revenue	168,169	149,994
Interest revenue	267	262
Total consolidated income	**168,436**	**150,256**
Earnings before net interest, tax, depreciation and amortisation ('EBITDA')	**28,206**	**16,510**
Depreciation expense	(3,537)	(3,163)
Amortisation expense	(3,518)	(2,413)
Total earnings before net interest and tax ('EBIT')	**21,151**	**10,934**
Net interest expense	(1,394)	(949)
Profit before tax	**19,757**	**9,985**
Income Tax expense	(7,049)	(3,257)
Profit for the year	**12,708**	**6,728**
Profit for the year attributable to:		
Members of the parent	**10,727**	**5,610**
Non-controlling interests	1,981	1,118
	12,708	**6,728**
Cashflow from operations	**14,302**	**13,623**

Directors' Report

Reported EBITDA of $28,206,000, was 71% better than 2015, with underlying EBITDA achieving $28,405,000, 29% better than 2015.

	2016 $'000	2015 $'000
Reported EBITDA	**28,206**	**16,510**
Adjustments to calculate underlying EBITDA:		
Transaction costs	595	1,995
Synergy costs	2,959	1,417
Gain on reassessment of non-controlling interests dividend liability	(586)	-
Gain on reassessment of contingent consideration liability	(1,024)	-
Gain on sale of IDNR business, net of transaction costs	(2,350)	-
Conversion of Tiger Pistol convertible notes	(162)	-
Contribution from IDNR business prior to sale	(144)	-
Contribution from acquisitions (assuming owned since 1 January)	599	3,100
Other non-operating (income)/expenses	312	(1,067)
Underlying EBITDA	**28,405**	**21,955**

Underlying net profit after tax ('Underlying NPAT') for the year ended 31 December 2016 was $14,344,000 (2015: $10,733,000), an increase of 34%. This resulted in strong underlying EPS growth in 2015, achieving 14.22 cents, an increase of 23.1% from the prior year.

Directors' Report

	2016 $'000	2015 $'000
Profit after tax attributable to members of the Parent	10,727	5,610
Adjustments to calculate underlying NPAT:		
Profit after tax attributable to non-controlling interests of Outware	1,839	896
Transaction costs (tax effected)	501	1,738
Synergy costs (tax effected)	2,071	992
Unwinding of discount on other financial liabilities	504	467
Gain on reassessment of non-controlling interests dividend liability	(586)	-
Gain on reassessment of contingent consideration liability	(1,024)	-
Sale of IDNR business, net of transaction costs and taxation	74	-
Conversion of Tiger Pistol convertible notes	(162)	-
Imputed interest income on convertible note receivables	(133)	-
Contribution from IDNR business prior to sale (tax effected)	(101)	-
Contribution from acquisitions (assuming 100% owned since 1 January) (tax effecte	416	2,097
Other non-operating (income)/expenses (tax effected)	218	(1,067)
Underlying NPAT	14,344	10,733

Outlook 2017 and beyond

The Group will continue to focus on the following six key areas in 2017:

- Integrating our acquisitions to generate operational, financial and cultural benefits throughout the organisation;
- Investment in our online marketing specialist capabilities across our sales and account management teams, with a focus on developing subject matter experts;
- Development of a deep understanding of our customers' needs through the use of data analytics in order to provide managed marketing solutions that are tailored to their individual needs as they progress along their online journey;
- Continue to innovate to develop easy-to-use solutions that simplify the process of establishing, managing and growing an online presence. We will continue to enhance and evolve our offering based on understanding deeply the needs of our customers.;
- Continued development of Enterprise Services managed services and new capabilities to offer clients a complete suite of digital services; and
- The implementation and upgrade of enterprise-grade support systems and shared services to support continued growth.

Risks review

Melbourne IT's ability to achieve its strategic objectives and secure its future financial prospects may be impacted by the following key risks:

- Competition – the online business world is rapidly evolving with a heightened environment of change characterised by disruptive technologies. Melbourne IT remains abreast of the competitive landscape by investing in new products and customer experience. The acquisitions of Netregistry and Uber Global assist in risk mitigation with

Directors' Report

access to a larger customer pool, increased skill sets, funds available for market investment and product enhancements.

- Markets – a material proportion of Melbourne IT revenue is derived from the performance of its reseller channel and ES professional services revenue from Corporate and Government customers. These revenue streams can be difficult to predict. Melbourne IT works closely with its customers to understand their challenges in order to mitigate these risks.
- Regulatory – Melbourne IT business operates in highly regulated global markets. Success can be impacted by changes to the regulatory environment. Melbourne IT plays an active role in consulting with regulators on changes which could impact our business.

Risk management

The Group takes a proactive approach to risk management and an active risk management plan is in place. The Group's approach to risk management is to determine the material areas of risk it is exposed to in running the organisation and to put in place plans to manage and/or mitigate those risks.

In addition, risk areas are reviewed by the Group's risk management staff, with the assistance of external advisors on specific matters, where appropriate.

Internal audit of key business processes is scheduled across the Group. The entire risk management plan is reviewed at least annually.

Significant changes in the state of affairs

On 18 March 2016, the Group successfully completed the capital raising of $15,000,000 which was substantially oversubscribed. The underwritten placement to professional and sophisticated investors was completed at an issue price of $2.00 per share. The 7,500,000 new shares issued ranked pari passu with existing ordinary shares on issue.

On 31 March 2016, the Group acquired 100% of InfoReady Pty Ltd (InfoReady), a leading data and analytics provider for the Enterprise Services market, for purchase consideration of $15,332,000 (including working capital adjustments) and three earn outs based on annual EBITDA performance for the three years from April 2016 to March 2019. The acquisition was funded through cash. The accounting for the acquisition in accordance with AASB 3 '*Business Combinations*' is as disclosed in Note D1(a) in the notes to the financial statements.

On 31 March 2016, the Group completed the sale of its International Domain Name Registration (IDNR) business for a sale consideration of US$6,000,000 (equivalent to AU$7,800,000). Refer to further details as disclosed in Note A7 in the notes to the financial statements.

The Group announced that the Board of Directors appointed Mr John Armstrong as a non-executive director effective 23 February 2016. Mr Armstrong is a company director and financial professional, with over 25 years' experience in various financial and commercial management roles. Mr Armstrong succeeded Mr Robert Stewart as Chairman of the ARMC. Mr Robert Stewart retired from his directorship at the Annual General Meeting held on 27 May 2016.

Melbourne IT announced the appointment of Ms Gail Pemberton as a non-executive director effective 27 May 2016. Ms Pemberton has more than 30 years of executive experience in the financial services industry with a particular focus on the banking and wealth management sectors and the technology and operations that underpin them. Ms Pemberton was appointed chairperson on 1 February 2017.

Other than as stated above, there have been no other significant changes in the state of affairs during the year ended 31 December 2016.

Significant events after balance date

On 22 February 2017, the directors declared a final dividend of 6.0 cents per ordinary share, franked at 100%, amounting to $6,052,000. The expected payment date of the dividend is 28 April 2017.

Directors' Report

On 16 February 2017, the Group entered into a Deed of Variation and Option Exercise with the owners of the non-controlling interest of Outware to purchase the remaining 24.9% of share capital for a total consideration of $28,692,000. Of the consideration paid, $1,000,000 will be held in escrow in the form of shares in Melbourne IT Group, and $2,683,000 will be held in escrow in cash until 31 December 2017, contingent on the employment of the vendors of the non-controlling interest by the Group until that date. This will extinguish the Group's put option and dividend liability to non-controlling interests in Outware. No further payment is due to the vendors of Outware. The total consideration paid for Outware (net of cash acquired) is $60,615,000, implying forward EBITDA multiple of 4.9 times.

The acquisition of the remaining non-controlling interest has been brought forward in order to accelerate the integration of the Outware operations into the Group.

Other than the above, there has not been any other matter or circumstance in the interval between the end of the year and the date of this report that has materially affected or may materially affect the operations of the consolidated entity, the results of those operations or the state of affairs of the consolidated entity in subsequent financial periods.

Likely developments and expected results

For further information about the likely developments and expected results of the Group, refer to the 'Outlook 2017' section on page 32 of this report.

Indemnification and insurance of directors and officers

The Company has entered into a Deed of Insurance and Indemnity with each of the non-executive directors, certain officers and executive directors of controlled entities. Under the Deed, the Company has agreed to indemnify these directors and officers against any claim or for any costs which may arise as a result of work performed in their capacity as directors and officers, to the extent permitted by law.

During the financial year, the Company paid an insurance premium in respect of a Directors and Officers Liability Policy covering all directors and officers of the Company and related bodies corporate. The contract of insurance prohibits disclosure of the nature of the liability and the amount of the premium.

To the extent permitted by law, the Company has agreed to indemnify its auditors, Ernst & Young Australia, as part of the terms of its audit engagement agreement against claims by third parties arising from the audit (for an unspecified amount). No payment has been made to indemnify Ernst & Young during or since the financial year.

Performance rights

Unissued shares

As at the date of this report, there were 1,705,684 unissued ordinary shares under performance rights (2015: 1,388,914). Refer to Note E4 to the Financial Statements for further details of the performance rights outstanding. Option holders do not have any right, by virtue of the option rules, to participate in any share issue of the Company or any related body corporate or in the issue of any other registered scheme.

Shares issued as a result of the exercise of performance rights

No performance rights were vested/exercised during the year ended 31 December 2016 (2015: Nil).

During the financial year, there were 529,178 rights granted (2015: 1,177,383 rights).

Directors' Report

Directors' meetings

As at the date of this report, the Company had an Audit and Risk Management Committee ('ARMC') and a Human Resources, Remuneration and Nomination Committee ('HRRNC') of the Board of Directors.

The members of the ARMC are Mr J. Armstrong (Chairman), Mr S. Jones, Mr L. Bloch and Ms G. Pemberton.

The members of the HRRNC are Ms N. Sparks (Chairman), Mr T. Kiing, Ms G. Pemberton and Mr L. Bloch.

The Managing Director and Chief Executive Officer attends each ARMC and each HRRNC by invitation.

The below table shows the numbers of meetings of directors held during 2016. The table also shows the number of meetings attended by each director and the number of meetings each committee member was eligible to attend.

	Directors' Meetings		Meetings of Committees			
			ARMC (1)		HRRNC (2)	
No. of meetings held in 2016	16		5		3	
	Eligible	Attended	Eligible	Attended	Eligible	Attended
Mr Simon Jones	16	16	5	5	3	3
Mr Martin Mercer	16	16				
Mr Tom Kiing	16	16			3	3
Ms Naseema Sparks	16	15			3	3
Mr Larry Bloch	16	15	5	4	3	2
Mr John Armstrong	14	13	4	4		
Ms Gail Pemberton	10	10	3	3		
Mr Robert Stewart AM	6	6	2	2		

(1) Audit and Risk Management Committee.

(2) Human Resources, Remuneration and Nomination Committee.

Rounding

The amounts contained in this report and in the financial report have been rounded to the nearest $1,000 (where applicable) under the option available to the Company under ASIC *Corporations (Rounding in Financial / Directors' Report) Instrument 2016/191* (Instrument 2016/191). The Company is an entity to which the Class Order applies.

Corporate governance

In recognising the need for the highest standards of corporate behaviour and accountability, the directors of Melbourne IT Ltd support and have adhered to the principles of corporate governance.

The Company's Corporate Governance Statement is available on the Company's website (www.melbourneit.info).

Directors’ Report

Remuneration Report (Audited)

This Remuneration Report outlines the director and executive remuneration arrangements of the Company and the Group in accordance with the requirements of the *Corporations Act 2001* and its Regulations. For the purpose of this report Key Management Personnel ('KMP') of the Group are defined as those persons having the authority and responsibility for planning, directing and controlling the major activities of the Company and the Group, directly or indirectly.

In 2016, the Group implemented an organisational restructure, whereby the marketing, customer care and sales functions reported into the newly created position of Managing Director, SMB.

For the purposes of this report, the KMP in 2016 are Martin Mercer - Chief Executive Officer/Managing Director, Peter Findlay - Chief Financial Officer, Brett Fenton - Chief Technology Officer, Amy Rixon - Chief People Officer, Peter Wright - Managing Director, Enterprise Services (ES) and Emma Hunt - Managing Director, SMB.

Directors of the Company are also included in the definition of KMP.

Human Resources, Remuneration and Nomination Committee (HRRNC)

The HRRNC of the Board of Directors of the Company is responsible for determining and reviewing compensation policy and arrangements for directors, executives and staff.

The HRRNC assesses the appropriateness of the nature and amount of remuneration of directors and executives on a periodic basis by reference to relevant employment market conditions and the overall objective of ensuring maximum stakeholder benefit from the retention of a high quality, high performing directors and executive team.

Remuneration philosophy

The performance of the Company depends upon the quality of its directors, executives and staff. Our approach to remuneration is to aim to pay an appropriate market rate for the skills and capabilities we require now and in the future and to align, so far as possible, executive remuneration with the creation of wealth for shareholders.

We strive to provide meaningful and rewarding work for our people and consider that remuneration is an important component in our overall Employee Value Proposition. The objective of our remuneration philosophy is to attract and retain quality, motivated and skilled people, appropriately compensate team members, and motivate our people to deliver business outcomes.

In line with this, the Company’s remuneration strategy is structured to:

- Reward all staff fairly and reasonably and encourage engagement with the Company;
- Attract and retain high calibre executives;
- Link executive rewards to creation of shareholder wealth;
- Be easy to understand – for the Board, executives and shareholders;
- Have a significant portion of executive remuneration ‘at risk’, and dependent on meeting pre-determined performance criteria;
- Reward executives for the successful implementation of the company’s strategy, and
- Reinforce the values and culture of Melbourne IT.

Further details of the remuneration of KMP are also provided in Notes E3 and E4 to the Financial Statements.

Directors’ Report

Remuneration structure

In accordance with best practice corporate governance, the structure of non-executive director and executive remuneration is separate and distinct.

Non-executive director remuneration

Objective

The Board seeks to set aggregate remuneration at a level that provides the Company with the ability to attract and retain directors of the highest calibre, while incurring a cost that is acceptable to shareholders.

Structure

The Constitution and the ASX Listing Rules specify that the aggregate remuneration of non-executive directors shall be determined from time to time by a general meeting. The last determination was at the Annual General Meeting held on 20 May 2008 when shareholders approved an aggregate remuneration of $1,000,000 per year.

The amount of aggregate remuneration sought to be approved by shareholders and the manner in which it is apportioned amongst directors is reviewed periodically. The Board considers advice from external consultants, the fees paid to non-executive directors of comparable companies as well as company performance when undertaking the annual review process.

Fixed remuneration

Each director receives a fee for being a director of the Company. Each director is expected to be a member of at least one committee. An additional fee is paid for chairing a Board committee in recognition of the additional time commitment and responsibility required.

Non-executive directors have long been encouraged by the Board to hold shares in the Company (purchased by the directors on market). It is considered good governance for directors to have a stake in a Company on whose board they sit. Details of the shareholding as at the date of this report are disclosed on page 28 of the Directors' Report.

The remuneration of non-executive directors is reviewed annually and for the period ended 31 December 2016 is detailed below.

Structure

Details of the nature and amount of each element of the remuneration of each non-executive director of Melbourne IT Ltd for the financial year are as follows:

Directors' Report

2016 Directors	Short Term Salary & fees $	Post Employment Superannuation Contribution $	Total $
Mr Simon Jones	176,813	16,797	193,610
Mr Tom Kiing	76,875	7,303	84,178
Ms Naseema Sparks	86,875	8,253	95,128
Mr Larry Bloch	76,875	7,303	84,178
Mr John Armstrong (1)	71,490	6,792	78,281
Ms Gail Permberton (2)	45,731	4,344	50,075
Mr Robert Stewart AM (3)	36,198	3,439	39,637
Total 2016	**570,856**	**54,231**	**625,087**

(1) Appointed 23 February 2016.

(2) Appointed 27 May 2016.

(3) Retired 27 May 2016.

2015 Directors	Short Term Salary & fees $	Post Employment Superannuation Contribution $	Total $
Mr Simon Jones	176,813	16,797	193,610
Mr Tom Kiing	76,875	7,303	84,178
Ms Naseema Sparks	86,875	8,253	95,128
Mr Robert Stewart AM	86,875	8,253	95,128
Mr Larry Bloch	86,875	8,253	95,128
Total 2015	**514,313**	**48,859**	**563,172**

Directors' Report

Executive and senior manager remuneration

Objective

The Company aims to reward executives and senior managers with a level and mix of remuneration commensurate with their position and responsibilities within the Company so as to:

- Reward them for company, business unit and individual performance against targets set by reference to appropriate benchmarks;
- Align their interests with those of shareholders;
- Link reward with the strategic goals and performance of the Company; and
- Ensure total remuneration is competitive by market standards.

Structure

To assist in achieving these objectives, the HRRNC links the nature and amount of executive remuneration to the Company's financial and operational performance. The CEO and those directly reporting to the CEO have the opportunity to participate in the Short Term Incentive Plan as described on page 41, additionally, the CEO and Direct Reports to the CEO are also participants in the Long Term Incentive Plan as described on page 42.

Remuneration consists of the following key elements:

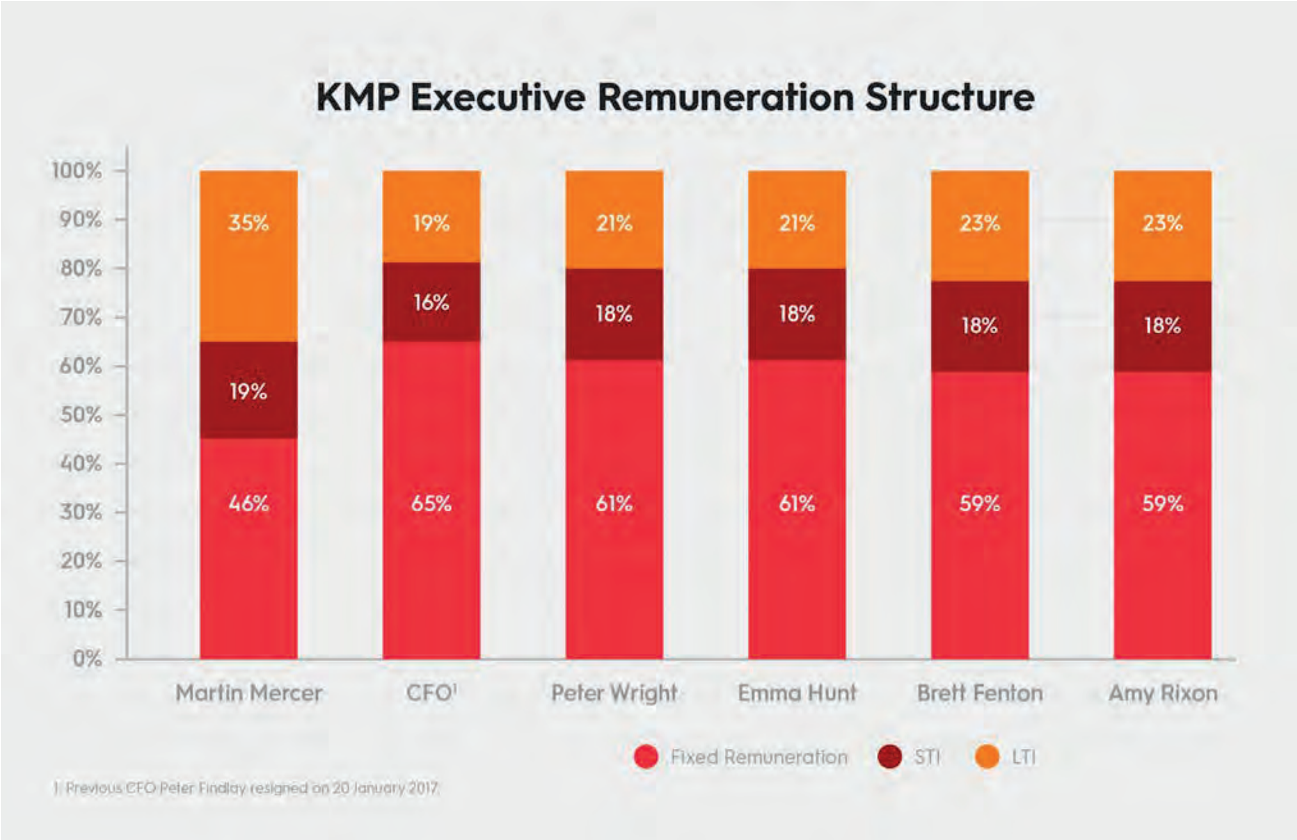
- Fixed Remuneration
  - All employees will have base salary and superannuation

- Variable Remuneration
  - In addition to fixed salary, some employees (based on role type and seniority) may have annual variable incentive, i.e. Short Term Incentives ('STI') based on company and individual performance.
  - Senior executives of the business may also have long term share plan incentives ('LTI') aligned with company performance.

- Other benefits
  - Depending on role type/ requirements and policy considerations, some additional benefits may also be included in an individual's remuneration package or offer. This could include parking, allowances, phone/ internet, etc.

The proportion of fixed and variable remuneration (potential short term and long term incentives) is established for executives by the HRRNC. The contracted remuneration mix for the KMPs for 2016 is expressed as a percentage of total remuneration (i.e. the sum of fixed and variable elements) and is set out in the chart on page 40. In addition, the table on page 44 details the actual fixed and variable remuneration components paid to the KMP.

Directors' Report



Directors' Report

Fixed remuneration

Objective

Fixed remuneration is reviewed annually by the HRRNC. The process consists of a review of company-wide, business unit and individual performance, relevant comparative remuneration in the market and internally, and where appropriate, external advice on policies and practices. The HRRNC has access to external advice independent of management.

Structure

Executives receive their fixed (primary) remuneration in cash.

The fixed remuneration component of the Key Management Personnel is detailed on page 44.

Variable remuneration – Short Term Incentives (STI)

Objective

The objective of the STI program is to link the achievement of the Group's operational and financial targets with the remuneration received by the executives charged with meeting those targets. The total potential STI available is set at a level so as to provide sufficient incentive to the executives to achieve the targets and such that the cost to the Group is reasonable in the circumstances.

Structure

The percentage of total remuneration that constitutes an executive's STI varies depending on the size of the role and its impact on the attainment of the Group's short term targets.

STI payments will only be made if the target relating to underlying earnings before interest, tax, depreciation, and amortisation ('EBITDA')[1] is met. In the event that the underlying EBITDA target is not achieved, then any STI payment is discretionary and will only be made if the executive has demonstrated exceptional performance in meeting the other targets.

In the event that the underlying EBITDA target is met then the total STI payment amount is determined by reference to an executive's performance against Group and Individual targets (collectively known as 'performance targets'). The Group targets include measures pertaining to underlying EBITDA, Revenue, People and Net Promoter Score. Individual targets comprise operational and financial measures pertaining to the executive's role and accountabilities. The chosen performance targets represent the key performance indicators for the short term success of the business and provide a framework for delivering long term value.

Achievement against the performance targets is assessed on an annual basis, and all payments are both reviewed and approved by the HRRNC. This assessment process usually occurs within three months of the end of our financial year. The limits that are applied to the STI payment ranges from nil to 150% of the Group measures, and nil to 100% of the Individual measures. During the year, 80% of the potential STI pool was paid in respect of the 31 December 2015 financial year. For the financial year ended 31 December 2016, 74% of the potential STI pool is payable (with payment occurring in 2017).

Less than 100% of the total STI pool was paid principally because the achievement against several of the Group targets was greater than 50% but less than 100%.

[1] Underlying EBITDA is calculated by removing the impact of material non-recurring items and treating all acquired and sold businesses as if the acquisition or disposal had occurred at the beginning of the year. Underlying EBITDA is the preferred measure because of the substantial restructuring that the Group has been undertaking, including acquiring and selling businesses.

Directors' Report

In addition, in 2016 the Board of Directors (following a recommendation from the HRRNC) exercised their discretion to pay an incentive to certain executives in recognition of their exceptional efforts relating to the acquisition of InfoReady and the sale of the International Domain Names Reseller business.

Variable remuneration – Long Term Incentives (LTI)

Objective

The objective of the LTI plan is to reward executives, senior management and staff in a manner that aligns this element of remuneration with the creation of shareholder wealth. As such, LTI grants are made to executives, senior management and staff who are able to influence the generation of shareholder wealth and thus have a direct impact on the Group's performance against the relevant long term performance hurdle.

Structure

LTI grants to executives are delivered in the form of performance rights.

Performance Rights Plan

Performance Rights issued since 1 January 2014 have two performance conditions; 50% of the Performance Rights will vest based on the increase in underlying earnings per share ('EPS'), and 50% will vest based on relative total shareholder return ('TSR') in comparison to a peer group from the S&P/ASX Small Ordinaries Index. These Performance Rights were granted with a zero exercise price. The Performance Rights vest on a sliding scale and the proportion of Rights that vest depends on the actual increase in EPS and the relative TSR performance. Performance is measured over the 36 month period from 1 January of the respective grant year to 31 December of the respective vesting year and will be settled in the equivalent number of ordinary shares of Melbourne IT.

Following the end of the performance period the Melbourne IT Board reviews the achievement against the performance conditions. The Board has a discretion to adjust the performance conditions or the number of rights that actually vest in order to ensure that eligible employees are not unfairly advantaged or disadvantaged. The Board considers that acquisitions properly executed are a legitimate avenue for the creation of shareholder wealth and that acquisitions do not, therefore, unfairly advantage eligible employees. Accordingly, the Board does not consider that this is a circumstance where it should or will exercise its discretion. Having said this, the Board has set and published clear criteria that any acquisition must satisfy and has clear capital management guidelines that ensure that the Company's balance sheet is protected.

Performance Rights relating to the year ended 31 December 2016 (hereafter referred to as 2016 LTI Plan) were granted to all eligible participants on 27 May 2016, which was approved by shareholders at the Annual General Meeting on 27 May 2016. The following sliding scale is applied to the exercise of the Rights in relation to the 2016 LTI Plan:

TSR Percentile Rank Achieved	Proportion of TSR Rights Vesting
>75th percentile	100%
>50.1 percentile and <75th percentile	Pro-rata allocation
<50 percentile	0%

Compound annual EPS growth	Proportion of EPS Rights Vesting
>12%	100%
>8% and <12%	Pro-rata allocation
<8%	0%

Performance Rights relating to the 31 December 2015 financial year (hereafter referred to as 2015 LTI Plan) were granted to all eligible staff on 30 March 2015, with the exception of the CEO. On 29 June 2015, the CEO received a grant of

Directors' Report

Performance Rights in respect of the 2015 LTI Plan, which was approved by shareholders at the Annual General Meeting on 27 May 2015. The following sliding scale is applied to the exercise of the Rights in relation to the 2015 LTI Plan:

TSR Percentile Rank Achieved	Proportion of TSR Rights Vesting
>75th percentile	100%
>50.1 percentile and <75th percentile	Pro-rata allocation
<50 percentile	0%

Compound annual EPS growth	Proportion of EPS Rights Vesting
>20%	100%
>12% and <20%	Pro-rata allocation
<12%	0%

The TSR performance condition is a relative measure and vesting depends on the comparative performance with an appropriate peer group of companies. The relative TSR performance hurdle is tested once at the end of the performance period and is based on the 60 trading day average share price prior to the start and end of the performance period. The EPS performance condition is an absolute measure.

The HRRNC adopts a three-step process in setting the underlying EPS performance condition.

- management prepares a three year forecast including a three year underlying EPS forecast;
- the HRRNC reviews this forecast and makes any adjustments that it considers appropriate; and
- the growth in EPS that is required to achieve the resulting underlying EPS target is then calculated (the starting point underlying EPS figure for calculating the hurdle growth rate is the underlying EPS figure for the immediately preceding year).

The table below sets out the relevant underlying EPS targets and the implied growth rates for the three most recent grants.

Grant Year	CAGR[1] %	Target EPS[2]	Actual EPS 2016	Actual EPS 2017	Actual EPS 2018	Vesting[3] %
2014	23[4]	13.93	14.22			100
2015	7[4,5]	11.55		N/A		N/A
2016	12	16.23			N/A	N/A

(1) This is the compound annual growth rate to achieve the three year underlying EPS target, based on the opening underlying EPS (reported number for the immediately prior year).

(2) This is the forecast underlying EPS target that was approved by the HRRNC and from which the hurdle rate is calculated.

(3) The percentage of the EPS component that has/will vested (Note: 50% of the rights vest if the EPS hurdle is achieved and the other 50% are subject to a relative TSR test).

(4) The growth in EPS required for the 2014 and 2015 rights to vest differs from the stated hurdle rates in the Notices of Meeting for the 2014 and 2015 AGMs. This difference came about because an estimate of the base EPS was used when calculating the hurdle rates included in the Notices of Meeting. An estimate was used because the audited accounts had not been prepared in time for the HRRNC meeting. When audited accounts were finalised, the actual base EPS differed from the estimate. While regrettable, this had no practical consequence, the target EPS was correctly determined and it is achievement of the target EPS that determines whether or not the rights vest. The timeline has now been changed to ensure that the calculation of the hurdle rate occurs after the audited accounts are finalized. As a result, the growth rate required for the 2016 grant to vest is the same as the hurdle rate in the Notice of Meeting for the 2016 AGM.

(5) While the growth rate required for the 2015 rights to vest is technically 7%, the actual growth rate will substantially exceed this. The underlying EPS at the end of 2016 was 14.22c. If there is no growth in underlying EPS in 2017 the 3 year CAGR (i.e. 2015 to 2017) in EPS will be 14%. If, however, the Company achieves the mid-point of its guidance range for underlying EPS at the end of 2017 the 3 year CAGR will be 19%. The hurdle rate in the Notice of Meeting for the 2015 AGM was a range of 12% (for 50% vesting) through to 20% (for 100% vesting).

Directors’ Report

Remuneration of executives of the company and the consolidated entity

Details of the nature and amount of each element of the total remuneration for each member of the Key Management Personnel for the year ended 31 December 2016 and 2015 are set out in the tables.

2016	Short term benefits			Post Employment benefits	Long term benefits	Share Based Payments	Other		
Executives	Salary & fees $	STI[(1)] $	Other[(2)] $	Super contribution $	Long service leave[(3)] $	Amortisation expense[(4)] $	Termination pay $	Total $	Performance related[(5)] %
Mr Martin Mercer	549,833	183,198	4,368	30,724	7,972	318,414	-	1,094,509	45.8%
Mr Peter Findlay[(6)]	361,129	69,328	6,404	25,572	8,958	21,233	-	492,624	18.4%
Mr Peter Wright	295,112	74,758	2,916	28,630	8,523	65,184	-	475,123	29.5%
Mrs Amy Rixon	209,086	43,670	2,880	19,823	2,893	48,329	-	326,681	28.2%
Mr Brett Fenton	216,145	58,776	2,880	20,900	4,225	75,190	-	378,116	35.4%
Ms Emma Hunt[(7)]	118,851	31,028	1,200	10,379	-	-	-	161,458	19.2%
Total 2016	**1,750,156**	**460,758**	**20,648**	**136,028**	**32,571**	**528,350**	**-**	**2,928,511**	

(1) Represent STIs accrued in relation to 2016 financial year.

(2) Includes the cost to the business of any non-cash business benefits provided.

(3) Comprises long service leave accrued during the year.

(4) Relates to the amortisation booked during the year in relation to the fair value of the 2014, 2015 and 2016 Performance Rights.

(5) Calculated as STI plus amortisation of performance rights, as a proportion of total remuneration. These two elements represent the at-risk and discretionary amount payable which will vary depending on the financial performance of the Company. They are in addition to the fixed remuneration.

(6) Mr Peter Findlay resigned from the Group and executive on 20 January 2017.

(7) Ms Emma Hunt was appointed to the executive on 15 August 2016. She holds the position of Managing Director, SMB.

Directors’ Report

2015	Short term benefits			Post Employment benefits	Long term benefits	Share Based Payments	Other		
Executives	Salary & fees $	STI[1] $	Other[2] $	Super contribution $	Long service leave[3] $	Amortisation expense[4] $	Termination pay $	Total $	'erformance related[5] %
Mr Martin Mercer	590,276	208,602	5,634	36,615	-	224,149	-	1,065,276	40.6%
Mr Peter Findlay	369,501	108,057	10,566	28,422	3,744	68,937	-	589,227	30.0%
Dr Bruce Tonkin	252,212	47,218	12,703	25,706	8,835	38,826	-	385,500	22.3%
Mr Peter Wright	295,867	78,366	5,368	29,663	4,827	41,865	-	455,956	26.4%
Ms Amy Rixon	185,918	37,495	5,368	17,971	-	34,968	-	281,720	25.7%
Mr Brett Fenton	218,016	58,183	5,368	20,900	4,214	55,269	-	361,950	31.3%
Ms Verity Meaghe	192,035	45,385	5,368	18,999	7,451	37,683	-	306,921	27.1%
Ms Catherine Hodgson-Croker	240,126	86,173	5,368	22,379	-	12,998	-	367,044	27.0%
Mr Simon Smith[6]	176,240	-	3,255	16,935	-	-	-	196,430	0.0%
Total 2015	**2,520,191**	**669,479**	**58,998**	**217,590**	**29,071**	**514,695**	**-**	**4,010,024**	

(1) Represent STIs accrued in relation to 2015 financial year and STIs paid to executives who worked on the acquisition of Outware.

(2) Includes the cost to the business of any non-cash business benefits provided.

(3) Comprises long service leave accrued during the year.

(4) Relates to the amortisation booked during the year in relation to the fair value of the 2014 and 2015 Performance Rights.

(5) Calculated as STI plus Amortisation of Performance Rights, as a proportion of total remuneration. These two elements represent the at-risk and discretionary amount payable which will vary depending on the financial performance of the Company. They are in addition to the fixed remuneration.

(6) Mr Simon Smith resigned from the Group and executive on 28 August 2015.

Employment contracts

The Managing Director and Chief Executive Officer, Mr Martin Mercer, is employed under an ongoing contract from 7 April 2014 and continues until such time that employment is terminated. Under the terms of the contract:

- He receives fixed remuneration plus superannuation per year. This remuneration will be reviewed annually.
- He is eligible for discretionary annual STI opportunity up to a maximum of 41% of fixed remuneration.
- He is eligible to participate in the LTI plans on terms determined by the Board, subject to receiving shareholders' approval.
- He may resign from this position and thus terminate the contract by giving six months' notice.
- The Company may terminate this employment contract by providing 12 months' notice.

All other executives are on standard contracts and are remunerated as stipulated in this report.

Performance rights: rights granted and rights vested during the year 2016

During the year ended 31 December 2016, there were 529,178 performance rights granted to the KMP (2015: 1,177,383).

Shares issued on exercise of rights

No performance rights were vested/exercised during the year ended 31 December 2016 (2015: Nil).

Directors’ Report

Performance rights granted/vested/exercised/forfeited as remuneration during the year 2016

	Rights granted	Value of rights granted[1] $	Value of rights vested/ exercised $	Number of rights forfeited	Value of rights forfeited $	Remuneration consisting of rights[2] %
Directors						
Mr Simon Jones	-	-	-	-	-	0.0%
Mr Martin Mercer	219,219	282,793	-	-	-	25.8%
Mr Robert Stewart AM	-	-	-	-	-	0.0%
Mr Tom Kiing	-	-	-	-	-	0.0%
Ms Naseema Sparks	-	-	-	-	-	0.0%
Mr Larry Bloch	-	-	-	-	-	0.0%
Mr John Armstrong	-	-	-	-	-	0.0%
Ms Gail Pemberton	-	-	-	-	-	0.0%
Executives						
Mr Peter Findlay[3]	79,327	102,332	-	144,066	159,934	-11.7%
Mr Peter Wright	54,231	69,958	-	-	-	14.7%
Ms Amy Rixon	31,071	40,082	-	-	-	12.3%
Mr Brett Fenton	46,327	59,762	-	-	-	15.8%
Ms Emma Hunt	-	-	-	-	-	0.0%
	430,175	**554,927**	**-**	**144,066**	**159,934**	

(1) Represents the grant date valuation multiplied by the number of performance rights granted. This cost is expensed over the three year performance period.

(2) The proportion of remuneration consisting of performance rights is not considered meaningful for leavers, due to the fact that the current year remuneration as reported in the table on page 44 includes the reversal of prior year share based payments amortisation.

(3) Mr Peter Findlay resigned from the Group and executive on 20 January 2017, and as such 159,934 were forfeited.

The maximum grant, which will be payable assuming that all service and performance criteria are met, is equal to the number of performance rights granted multiplied by the fair value at the vesting date. The minimum grant payable assuming that service and performance criteria are not met is zero.

Directors' Report

Rights holdings of Key Management Personnel as at 31 December 2016

	Opening balance	Rights granted	Rights vested/ exercised	Rights forfeited	Closing balance	Vested and exercisable at year end
Directors						
Mr Simon Jones	-	-	-	-	-	-
Mr Martin Mercer	581,862	219,219	-	-	801,081	-
Mr Robert Stewart AM	-	-	-	-	-	-
Mr Tom Kiing	-	-	-	-	-	-
Ms Naseema Sparks	-	-	-	-	-	-
Mr Larry Bloch	-	-	-	-	-	-
Mr John Armstrong	-	-	-	-	-	-
Ms Gail Pemberton	-	-	-	-	-	-
Executives						
Mr Peter Findlay	193,748	79,327	-	(144,066)	129,009	-
Mr Peter Wright	116,763	54,231	-	-	170,994	-
Ms Amy Rixon	95,670	31,071	-	-	126,741	-
Mr Brett Fenton	150,985	46,327	-	-	197,312	-
Ms Emma Hunt	-	-	-	-	-	
	1,139,028	**430,175**	**-**	**(144,066)**	**1,425,137**	**-**

Directors' Report

Shareholdings of Key Management Personnel as at 31 December 2016

	Opening balance	Granted as remuneration	Net change other(2)	Shares issued(3)	Closing balance
Directors					
Mr Simon Jones	155,935	-	1,266	-	157,201
Mr Martin Mercer	-	-	-	-	-
Mr Tom Kiing	5,721,488	-	-	-	5,721,488
Mr Robert Stewart AM(1)	810,784	-	15,168	-	825,952
Ms Naseema Sparks	-	-	6,612	-	6,612
Mr Larry Bloch	9,208,363	-	250,000	-	9,458,363
Mr John Armstrong	-	-	-	-	-
Ms Gail Pemberton	-	-	51,285	-	51,285
Executives					
Mr Peter Findlay	114,333	-	(114,333)	-	-
Mr Peter Wright	76,222	-	(76,222)	-	-
Ms Amy Rixon	-	-	-	-	-
Mr Brett Fenton	-	-	-	-	-
Ms Emma Hunt	-	-	-	-	-
	16,087,125	**-**	133,776	**-**	**16,220,901**

(1) Mr Robert Stewart AM retired on 27 May 2016 and his closing balance represents his holdings at this date.

(2) On market transactions

(3) Represents shares issued to satisfy Performance Rights Plans

Employees

The consolidated entity employed 559 full time equivalent ('FTE') employees as at 31 December 2016 (2015: 505 FTE).

Auditor independence and non-audit services

The Directors have received an independence declaration from the auditor of Melbourne IT Ltd, as shown on page 127.

Directors' Report

Non-audit services

The following non audit services were provided by the Group's auditor, Ernst & Young. The directors are satisfied that the provision of non-audit services is compatible with general standards of independence for auditors imposed by the *Corporations Act 2001*. The nature and scope of each type of non-audit service provided means that auditor independence was not compromised.

Ernst & Young received or are due to receive the following amounts for the provision of non-audit services:

	$
Taxation advice services	55,275
Assurance related services	113,676
	168,951

Signed in accordance with a resolution of the directors.

Gail Pemberton (Chair)

Sydney, 30 March 2017

Directors’ Report

In accordance with a resolution of the directors of Melbourne IT Ltd, I state that:

(1) In the opinion of the directors:

(a) the financial statements and notes of Melbourne IT Ltd for the financial year ended 31 December 2016 are in accordance with the *Corporations Act 2001*, including

(i) giving a true and fair view of its financial position as at 31 December 2016 and of its performance for the year ended on that date;

(ii) complying with Accounting Standards (including the Australian Accounting Interpretations) and *Corporations Regulations 2001*; and

(b) the financial statements and notes also comply with International Financial Reporting Standards as disclosed in Notes to the Financial Statements.

(c) there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.

(2) This declaration has been made after receiving the declarations required to be made to the directors in accordance with section 295A of the *Corporations Act 2001* for the financial year ended 31 December 2016.

(3) In the opinion of the directors, as at the date of this declaration, there are reasonable grounds to believe that the members of the Closed Group, as identified in Note E9, as parties to a Deed of Cross Guarantee, will be able to meet any obligations or liabilities to which they are, or may become subject to, under the deed as described in Note E8.

On behalf of the Board

Gail Pemberton (Chair)

Sydney, 30 March 2017

Financial Statements

Consolidated statement of financial position
As at 31 December 2016

ASSETS	Notes	2016 $'000	2015 $'000
Current Assets			
Cash and cash equivalents	E1	16,426	12,370
Trade and other receivables	B1	18,093	12,259
Prepayment of domain name registry charges		6,851	9,384
Current tax asset		-	83
Derivative financial instruments	C7	4	-
Other assets		4,484	3,624
Total Current Assets		**45,858**	**37,720**
Non-Current Assets			
Plant and equipment	B2	6,739	7,426
Intangible assets	B3	222,036	204,805
Deferred tax assets	A3	4,438	5,298
Prepayment of domain name registry charges		3,392	5,376
Non-current financial assets	B4	1,795	1,995
Other assets		38	168
Total Non-Current Assets		**238,438**	**225,068**
TOTAL ASSETS		**284,296**	**262,788**
LIABILITIES			
Current Liabilities			
Trade and other payables	B5	18,804	17,077
Interest-bearing loans and borrowings	C4	92	198
Provisions	B6	3,461	3,321
Current tax liabilities		1,684	-
Derivative financial instruments	C7	-	117
Income received in advance		24,883	28,914
Other financial liabilities	C6	31,089	18,885
Total Current Liabilities		**80,013**	**68,512**
Non-Current Liabilities			
Interest-bearing loans and borrowings	C4	36,536	30,144
Deferred tax liabilites	A3	2,980	2,775
Provisions	B6	803	546
Income received in advance		10,067	12,954
Other financial liabilities	C6	8,315	27,274
Total Non-Current Liabilities		**58,701**	**73,693**
TOTAL LIABILITIES		**138,714**	**142,205**
NET ASSETS		**145,582**	**120,583**
EQUITY			
Contributed equity	C2(a)	51,026	35,629
Foreign currency translation reserve	C3	(593)	(573)
Options reserve	C3	1,398	776
Hedging reserve	C3	3	(82)
Other reserve	C3	8,523	3,646
Available-for-sale (AFS) reserve	C3	-	498
Retained earnings		85,074	80,379
Equity attributable to Equity holders of the parent		145,431	120,273
Non-controlling interest		151	310
TOTAL EQUITY		**145,582**	**120,583**

The above consolidated statement of financial position should be read in conjunction with the accompanying notes.

Financial Statements

Consolidated statement of comprehensive income
For the year ended 31 December 2016

	Notes	2016 $'000	2015 $'000
Continuing operations			
Revenue	A1	168,436	150,256
Registry, hosting and sundry other product costs		(74,198)	(66,312)
Gross profit		**94,238**	**83,944**
Other income	A8	1,610	-
Salaries and employee benefit expenses	A2(a)	(54,162)	(50,337)
Depreciation expenses	A2(b)	(3,537)	(3,163)
Amortisation of identifiable intangible assets	A2(c)	(3,518)	(2,413)
Transaction costs relating to the acquisitions	D1	(595)	(1,995)
Finance costs	A2(d)	(3,125)	(2,741)
Other expenses	A2(e)	(13,504)	(13,310)
Gain on sale of IDNR business, net of transaction costs	A7	2,350	-
Profit before tax		**19,757**	**9,985**
Income tax expense	A3	(7,049)	(3,257)
Profit for the year		**12,708**	**6,728**
Other comprehensive income			
Items that are reclassified to the profit or loss:			
Currency translation differences		(20)	85
Items that may be reclassified to the profit or loss:			
Net gains/(losses) on cashflow hedges (net of tax)		85	(113)
Net gain on available-for-sale financial assets		48	498
Recycling of AFS reserve upon derecognition of AFS financial asset		(546)	-
Other comprehensive income/ (loss) for the year, net of tax		(433)	470
TOTAL COMPREHENSIVE INCOME FOR THE YEAR		**12,275**	**7,198**
Profit for the year attributable to:			
Equity holders of the parent		10,727	5,610
Non-controlling interests		1,981	1,118
		12,708	**6,728**
Total comprehensive income attributable to:			
Equity holders of the parent		10,294	6,080
Non-controlling interests		1,981	1,118
		12,275	**7,198**

Earnings per share		2016 Cents	2015 Cents
Basic earnings per share	A5	10.86	6.04
Diluted earnings per share	A5	10.67	5.95

The above consolidated statement of comprehensive income should be read in conjunction with the accompanying notes.

Financial Statements

Consolidated statement of changes in equity
For the year ended 31 December 2016

	Foreign currency reserve	Options reserve	Hedging reserve	Other reserves	AFS reserve	Contributed equity	Retained earnings	Total	Non-controlling interest	Total equity
	$'000	$'000	$'000	$'000	$'000	$'000	$'000	$'000	$'000	$'000
As at 1 January 2016	**(573)**	**776**	**(82)**	**3,646**	**498**	**35,629**	**80,379**	**120,273**	**310**	**120,583**
Profit for the year	-	-	-	-	-	-	10,727	**10,727**	1,981	**12,708**
Fair value of AFS financial assets	-	-	-	-	48	-	-	**48**	-	**48**
Derecognition of AFS financial asset	-	-	-	-	**(546)**	-	-	**(546)**	-	**(546)**
Other comprehensive income	(20)	-	85	-	-	-	-	**65**	-	**65**
Total comprehensive income for the year	(20)	-	85	-	(498)	-	10,727	**10,294**	1,981	**12,275**
Transactions with owners in their capacity as owners:										
Share based payment	-	622	-	-	-	-	-	**622**	-	**622**
Dividend reinvestment plan	-	-	-	-	-	821		**821**	-	**821**
Capital raising	-	-	-	-	-	14,576		**14,576**	-	**14,576**
Equity dividends	-	-	-	-	-	-	(6,032)	**(6,032)**	(300)	**(6,332)**
Transfer to other reserve	-	-	-	4,877	-	-	-	**4,877**	(4,877)	**-**
Transfer from/(to) financial liabilities	-	-	-	-	-	-	-	**-**	3,037	**3,037**
As at 31 December 2016	**(593)**	**1,398**	**3**	**8,523**	-	**51,026**	**85,074**	**145,431**	**151**	**145,582**
As at 1 January 2015	**(658)**	**5,321**	**31**	**-**	**-**	**35,629**	**74,357**	**114,680**	**88**	**114,768**
Profit for the year	-	-	-	-	-	-	5,610	**5,610**	1,118	**6,728**
Other comprehensive income	85	-	(113)	-	498	-	-	**470**	-	**470**
Total comprehensive income for the year	85	-	(113)	-	498	-	5,610	**6,080**	1,118	**7,198**
Transactions with owners in their capacity as owners:										
Share based payment	-	514	-	-	-	-	-	**514**	-	**514**
Equity dividends	-	-	-	-	-	-	(4,647)	**(4,647)**	-	**(4,647)**
Acquisition of subsidiary (Note D1)	-	-	-	-	-	-	-	**-**	45,266	**45,266**
Transfer to other reserve	-	-	-	3,646	-	-	-	**3,646**	(3,646)	**-**
Transfer from/(to) financial liabilities	-	-	-	-	-	-	-	**-**	(42,516)	**(42,516)**
Transfer to/(from) options reserve	-	(5,059)	-	-	-	-	5,059	**-**	-	**-**
As at 31 December 2015	**(573)**	**776**	**(82)**	**3,646**	**498**	**35,629**	**80,379**	**120,273**	**310**	**120,583**

The above consolidated statement of changes in equity should be read in conjunction with the accompanying notes.

Financial Statements

Consolidated statement of cash flows
For the year ended 31 December 2016

	Notes	2016 $'000	2015 $'000
Cash flows from operating activities			
Receipt of service revenue and recoveries		179,286	163,004
Payments to suppliers and employees		(158,509)	(145,317)
Interest received		134	262
Interest paid		(1,157)	(754)
Bank charges and credit card merchant fees		(1,464)	(1,530)
Income tax refunds		1,989	835
Income tax paid		(5,977)	(2,877)
Net cash flows from operating activities	E1	**14,302**	**13,623**
Cash flows from investing activities			
Purchase of plant and equipment and intangible assets		(4,874)	(5,782)
Purchase of financial asset	B4	-	(247)
Proceeds from sale of IDNR business, net of transaction costs		7,424	-
Acquisition of InfoReady	D1(a)	(15,382)	-
Acquisition of Uber	D1(b)	-	(14,909)
Acquisition of Outware, net of cash acquired	D1(c)	(10,622)	(21,301)
Transaction costs relating to acquisitions	D1	(616)	(1,974)
Net cash flows (used in) investing activities		**(24,070)**	**(44,213)**
Cash flows from financing activities			
Proceeds from borrowings	C4	10,600	33,500
Repayment of borrowings	C4	(4,100)	(3,500)
Proceeds from capital raising	C2	15,000	-
Transaction costs on capital raising	C2	(605)	-
Payment of dividend to equity holders of the parent		(5,211)	(4,647)
Payment of dividend to non-controlling interests		(1,629)	(224)
Payment of finance lease liabilities		(214)	(260)
Net cash flows from financing activities		**13,841**	**24,869**
Net increase/ (decrease) in cash and cash equivalents		4,073	(5,721)
Net foreign exchange differences		(17)	5
Cash and cash equivalents at beginning of year		12,370	18,086
CASH AND CASH EQUIVALENTS AT END OF YEAR	E1	**16,426**	**12,370**

The above statement of cash flows should be read in conjunction with the accompanying notes.

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For the year ended 31 December 2016

About this report

This is the financial report of Melbourne IT Ltd ('the Company' or 'Melbourne IT') and of its controlled entities (collectively 'the Group') for the year ended 31 December 2016. The financial report was authorised for issue in accordance with a resolution of the directors on 30 March 2017.

It is a general-purpose financial report, which has been prepared in accordance with the requirements of the Corporations Act 2001, Australian Accounting Standards, and other authoritative pronouncements of the Australian Accounting Standards Board. The financial report complies with Australian Accounting Standards and International Financial Reporting Standards ('IFRS') as issued by the International Accounting Standards Board.

Melbourne IT Ltd is a company limited by shares incorporated and domiciled in Australia whose shares are publicly traded on the Australian Stock Exchange. The Company is a for-profit entity.

From this year onwards, the Group's financial report have been presented in a more streamlined manner by changing the format and layout to simplify the information disclosed and make it more relevant to users. The notes to the financial statements have been grouped into similar sections. Key accounting policies, along with key judgements and estimates, have been moved into the notes to which they are related.

Basis of preparation

The financial report has been prepared on a historical cost basis, except for derivative financial instruments that have been measured at fair value and certain assets where an impairment loss has been charged. The carrying values of recognised assets and liabilities that are hedged with fair value hedges are adjusted to record changes in the fair values attributable to the risks that are being hedged.

The financial report is presented in Australian dollars and all values are rounded to the nearest thousand dollars ($'000), unless otherwise stated, under the option available to the Company under ASIC *Corporations (Rounding in Financial/Directors' Report)* Instrument 2016/191 (Instrument 2016/191). The Company is an entity to which this Instrument 2016/191 applies.

The financial report has been prepared on a going concern basis, which assumes the Group will be able to meet its obligations as and when they fall due. The Group's current liabilities exceed current assets by $34,155,000 as at 31 December 2016 (2015: $30,792,000). This mainly arises due to the revenue recognition policy for domain names resulting in income in advance of $24,883,000 being recognised as a current liability. Furthermore, a $29,828,000 liability relating to the fair value of the put liability for the earn out payable to the vendors of Outware on completion of the 30 June 2017 results has also been recognised as a current liability. The Group has undrawn bank facilities of $47,100,000 which the Group can utilise to pay this earn out amount if necessary. Refer to Note C4.

Significant accounting policies

Accounting policies are selected and applied in a manner that ensures that the resulting financial information satisfies the concept of relevance and reliability, thereby ensuring that the substance of the underlying transactions or other events is reported.

Notes to the Financial Statements

(a) Basis of consolidation

The consolidated financial statements comprise the financial statements of Melbourne IT Ltd and its subsidiaries as at 31 December each year ('the Group'). The Group controls a subsidiary if and only if the Group has:

- power over the subsidiary (i.e. existing rights that give it the current ability to direct the relevant activities of the subsidiary);
- exposure, or rights, to variable returns from its involvement with the subsidiary; and
- the ability to use its power over the subsidiary to affect its returns."

The financial statements of subsidiaries are prepared for the same reporting period as the parent company, using consistent accounting policies. In preparing the consolidated financial statements, all intercompany balances and transactions, including unrealised profits arising from intra-group transactions, have been eliminated in full.

Subsidiaries are fully consolidated from the date on which control is transferred to Melbourne IT Ltd and cease to be consolidated from the date on which control is transferred out of Melbourne IT Ltd.

Investments in subsidiaries held by Melbourne IT Ltd are accounted for at cost in the separate financial statements of the parent entity less any impairment charges. Dividends received from subsidiaries are recorded as a component of other revenues in the separate income statement of the parent entity, and do not impact the recorded cost of the investment. Upon receipt of dividend payments from subsidiaries, the parent will assess whether any indicators of impairment of the carrying value of the investment in the subsidiary exist. Where such indicators exist, to the extent that the carrying value of the investment exceeds its recoverable amount, an impairment loss is recognised.

The acquisition of subsidiaries is accounted for using the acquisition method of accounting. The acquisition method of accounting involves recognising at acquisition date, separately from goodwill, the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquiree. The identifiable assets acquired and the liabilities assumed are measured at their acquisition date fair values. The difference between the above items and the fair value of the consideration (including the fair value of any pre-existing investment in the acquiree) is goodwill or a discount on acquisition.

After initial recognition, goodwill is measured at cost less any accumulated impairment losses. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group’s cash-generating units that are expected to benefit from the combination, irrespective of whether other assets or liabilities of the acquirer are assigned to those units. Where goodwill forms part of a cash-generating unit and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash-generating unit retained.

Acquisitions of subsidiaries that includes put options to acquire non-controlling interests in the future are accounted for in accordance with AASB 10 *Consolidated Financial Statements* (AASB 10). During the period the non-controlling interests put options remain unexercised, the non-controlling interests are calculated and immediately derecognised as though it was acquired at that date. A financial liability with respect to put options is recognised in accordance with AASB 139 *Financial Instruments: Recognition and Measurement*. The difference between derecognition of the non-controlling interests and recognition of the financial liabilities is accounted for as an equity transaction, and disclosed as a separate reserve within equity (refer to 'Other Reserves' disclosed in the Statement of Changes in Equity).

Notes to the Financial Statements

Where there is loss of control of a subsidiary, the consolidated financial statements include the results for the part of the reporting period during which Melbourne IT Ltd has control. A change in the ownership interest of a subsidiary that does not result in a loss of control, is accounted for as an equity transaction.

On the loss of control of a subsidiary, the Group derecognises the assets and liabilities of the subsidiary, and the other components of equity related to the subsidiary. Any surplus or deficit arising on the loss of control is recognised in profit or loss.

(b) Foreign currency transactions

Both the functional and presentation currency of Melbourne IT Ltd and its Australian subsidiaries is Australian dollars (AUD).

Transactions in foreign currencies are initially recorded in the functional currency at the exchange rates ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the rate of exchange ruling at the reporting date. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate as at the date of the initial transaction.

The functional currency of each overseas subsidiary is as follows:

Investment in New Zealand subsidiary	- NZD (New Zealand Dollar)
Investment in US subsidiaries	- USD (United States Dollar)

The assets and liabilities of these overseas subsidiaries are translated into the presentation currency of Melbourne IT Ltd at the rate of exchange ruling at the reporting date and the statement of comprehensive income is translated at the weighted average exchange rates for the period.

The exchange differences arising on retranslation are taken directly to other comprehensive income. On disposal of a foreign entity, the deferred cumulative amount recognised in other comprehensive income relating to that particular foreign operation is recognised in the determination of profit and loss for the year.

On consolidation, exchange differences arising from the translation of any net investment in foreign entities, and of borrowings and other financial instruments designed as hedges of such investments are taken to the foreign currency translation reserve in equity. When a foreign operation is sold or any borrowings forming part of the net investment are repaid, a proportionate share of such exchange differences are recognised in the Statement of Comprehensive Income, as part of the gain on sale or loss on sale where applicable.

(c) Financial assets

(i) Recognition and measurement

Financial assets are classified, at initial recognition, as financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments, available for sale ('AFS') financial assets, or as derivatives designated as hedging instruments in an effective hedge, as appropriate.

Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss include financial assets held for trading and financial assets designated upon initial recognition at fair value through profit or loss. Derivatives, including separated embedded derivatives, are also classified as held for trading unless they are designated as effective hedging instruments as defined by AASB 139. Financial

Notes to the Financial Statements

assets at fair value through profit or loss are carried in the statement of financial position at fair value with net changes in fair value presented in the statement of profit or loss.

Available-for-sale (AFS) financial assets

AFS financial assets include equity investments and debt securities. Equity investments classified as AFS are those that are neither classified as held for trading nor designated at fair value through profit or loss.

After initial measurement, AFS financial assets are subsequently measured at fair value with unrealised gains or losses recognised as other comprehensive income ('OCI') and credited in the AFS reserve until the investment is derecognised, at which time the cumulative gain or loss is recognised in other operating income in the statement of profit or loss, or the investment is determined to be impaired when the cumulative loss is reclassified from the AFS reserve to the statement of profit or loss in finance costs. Interest earned while holding AFS financial assets is reported as interest income using the effective interest rate ('EIR') method in the statement of profit or loss.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments which are not quoted in an active market. After initial measurement, such financial assets are measured at amortised cost using the EIR method, less impairment. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees or costs that are an integral part of the EIR. The EIR amortisation is included in finance income in the statement of profit or loss. The losses arising from impairment are recognised in the statement of profit or loss in finance costs for loans and other operating expenses for receivables.

(ii) Impairment of financial assets

The Group assesses, at each reporting date, whether there is objective evidence that a financial asset or a group of financial assets is impaired. An impairment exists if one or more events that has occurred since the initial recognition of the asset (an incurred ‘loss event’) has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that the debtor or a group of debtors is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganisation and observable data indicating that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

Financial assets carried at amortised cost

For financial assets carried at amortised cost, the Group first assesses whether impairment exists individually for financial assets that are individually significant, or collectively for financial assets that are not individually significant. If the Group determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognised are not included in a collective assessment of impairment.

The amount of any impairment loss identified is measured as the difference between the asset’s carrying amount and the present value of estimated future cash flows (excluding future expected credit losses that have not yet been incurred). The present value of the estimated future cash flows is discounted at the financial asset’s original EIR.

Notes to the Financial Statements

Available-for-sale ('AFS') financial assets

For AFS financial assets, the Group assesses at each reporting date whether there is objective evidence that an investment or a group of investments is impaired.

In the case of equity investments classified as AFS, objective evidence would include a significant or prolonged decline in the fair value of the investment below its cost. 'Significant' is evaluated against the original cost of the investment and 'prolonged' against the period in which the fair value has been below its original cost. When there is evidence of impairment, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that investment previously recognised in the statement of profit or loss – is removed from OCI and recognised in the statement of profit or loss. Impairment losses on equity investments are not reversed through the statement of profit or loss; increases in their fair value after impairment are recognised directly in OCI.

The determination of what is 'significant' or 'prolonged' requires judgement. In making this judgement, the Group evaluates, among other factors, the duration or extent to which the fair value of an investment is less than its cost.

(d) Financial liabilities

Financial liabilities are classified, at initial recognition, as financial liabilities at fair value through profit or loss, loans and borrowings, payables or as derivatives designated as hedging instruments in an effective hedge, as appropriate. All financial liabilities are recognised initially at fair value and, in the case of loans and borrowings and payables, net of directly attributable transaction costs.

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires. When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as the derecognition of the original liability and the recognition of a new liability. The difference in the respective carrying amounts is recognised in the statement of profit or loss.

(e) Prepayment of domain name registry charges

Domain name registry charges are deferred in the Statement of Financial Position and are recognised in the Statement of Comprehensive Income using the same principles as revenue from the sale of domain names, as explained in accounting policy in Note A1.

Significant accounting estimates and judgements

The preparation of the financial statements requires management to make judgements, estimates and assumptions that affect reported amounts in the financial statements. Management continually evaluates its judgements and estimates in relation to assets, liabilities, contingent liabilities, revenues and expenses. Management bases its judgements and estimates on historical experience and on other various factors it believes to be reasonable under the circumstances, the result of which form the basis of the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions and conditions.

Management has identified the following critical accounting policies for which significant judgements, estimates and assumptions are made. Actual results may differ from these estimates under different assumptions and conditions and may materially affect financial results or the financial position reported in future periods.

Notes to the Financial Statements

Information on significant estimates and judgements considered when applying the accounting policies can be found in the following notes:

Accounting estimates and judgements	Note
Taxation	A3
Impairment of goodwill and intangibles and useful lives	B3
Convertible note receivables	B4
Put options liability and contingent consideration liability	C6
Control of Outware Systems Pty Ltd	D2
Share based payment transactions	E4

Notes to the Financial Statements

Section A: Financial performance

A1. Revenue

	2016	2015
	$'000	$'000
Registration revenue	44,916	55,932
Solutions, hosting & services	123,253	94,041
Other revenue	-	21
Total revenue excluding interest income	**168,169**	**149,994**
Interest revenue	267	262
Total consolidated revenue	**168,436**	**150,256**

Revenue recognition

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the entity and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised:

Rendering of services - domain names

Revenue is recognised by reference to percentage of completion method. The percentage of completion is determined by reference to the extent of services performed to date on the agreement as a percentage of total services to be performed under the agreement. Revenue is recognised in the financial period in which services are rendered. Where cash has been received for services yet to be performed pursuant to the agreement, the amount has been classified in the statement of financial position as "Income received in advance".

The following table summarises the domain name registration revenue and registry cost recognition policy for the Group:

Length of Registration	First month	Per other month
1 Year	78.00%	2.00%
2 Years	54.00%	2.00%
3 Years	36.00%	1.83%
4 Years	27.00%	1.55%
5 Years	21.60%	1.33%
6 Years	18.00%	1.15%
7 Years	15.43%	1.02%
8 Years	13.50%	0.91%
9 Years	12.00%	0.82%
10 Years	10.80%	0.75%

Notes to the Financial Statements

Rendering of services

Revenue from provision of other services is recognised when the services are performed or by reference to the stage of completion. Stage of completion is measured by reference to labour hours incurred to date as a percentage of total estimated labour hours for each contract.

Interest

Revenue is recognised as the interest accrues (using the effective interest method, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial instrument) to the net carrying amount of the financial asset.

Dividend income

Revenue is recognised when the shareholder's right to receive the payment is established.

A2. Expenses

		2016 $'000	2015 $'000
(a)	Salaries and employee benefits expense		
Included in salaries and employee benefits expenses:			
	Expensing of share-based payments	622	514
	Superannuation expense	3,824	3,154
(b)	Depreciation expense		
	Fit out	236	127
	Plant and equipment	3,250	3,000
	Furniture	51	36
Total depreciation of non-current assets		3,537	3,163
(c)	Amortisation of identifiable intangible assets		
	Capitalised software	1,935	1,607
	Customer contracts	1,548	806
	Marketing related intangibles	35	-
Total amortisation of identifiable intangible assets		3,518	2,413
(d)	Finance costs		
	Bank charges and credit card merchant fees	1,464	1,530
	Interest expense on debt and borrowings	1,157	744
	Unwinding of discount on other financial liabilities	504	467
Total finance costs		3,125	2,741

Notes to the Financial Statements

	2016 $'000	2015 $'000
(e) Other expenses		
Included in other expenses:		
Premises	3,605	3,452
Training and recruitment	1,597	1,111
Communications	1,012	1,308
Marketing	2,360	2,832
Equipment	2,462	2,480
Finance & legal	1,471	1,302
Foreign exchange	17	241
Bad debts and doubtful debts	(172)	337
Fair value of derivative financial asset	48	-
Recycling of AFS reserve upon derecognition of available-for-sale financial asset	(546)	-

Notes to the Financial Statements

A3. Income tax

	2016 $’000	2015 $’000
The major components of income tax expense are:		
(a) Statement of comprehensive income		
Current income tax		
Current income tax charge	5,887	2,340
Adjustments in respect of current income tax of previous years	(78)	57
Deferred income tax		
Relating to origination and reversal of temporary differences	1,240	860
Income tax expense reported in the statement of comprehensive income	**7,049**	**3,257**
(b) Statement of changes in equity		
Deferred income tax related to items charged or credited directly to equity		
Net gain on revaluation of cash flow hedges	(1)	35
Income tax expense reported in equity	**(1)**	**35**
(c) A reconciliation between tax expense and the product of accounting profit before income tax, multiplied by the Group's applicable income tax rate is as follows:		
Accounting profit before income tax	19,757	9,985
At the Group's statutory income tax rate of 30% (2015: 30%)	5,927	2,996
Adjustments in respect of current income tax of previous years	(78)	57
Non-deductible expenses	190	513
Other non operating income	(483)	-
Unwinding of discount on other financial liabilities	152	140
Goodwill allocated to gain on sale of IDNR business	1,719	-
Estimated R&D tax incentive claims	(377)	(510)
Other	(1)	61
Income tax expense at the effective income tax rate	**7,049**	**3,257**
Income tax expense reported in the statement of comprehensive income	**7,049**	**3,257**

Notes to the Financial Statements

	2016 $'000	2015 $'000
(d) Deferred tax assets and liabilities		
Deferred tax assets at 31 December relate to the following:		
Doubtful debts provision	234	308
Employee benefits and make good	1,278	1,153
Accruals	1,253	1,132
Unrealised foreign exchange losses	260	492
Transformation asset	319	908
Blackhole expenditure	278	204
Carry forward tax losses	784	999
Other	32	102
	4,438	**5,298**
Deferred tax liabilities at 31 December relate to the following:		
Intangible assets	2,709	2,374
Unrealised foreign exchange gains	238	373
Other	33	28
	2,980	**2,775**

As at 31 December 2016, Melbourne IT Group had unused carry forward tax losses of $2,614,000 (2015: $3,329,000). These carry forward tax losses arose on the acquisition of Uber Global Pty Ltd.

Current taxes

Current tax assets and liabilities for the current period are measured at the amount expected to be recovered from or paid to the taxation authorities based on the current period's taxable income. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted at the reporting date.

Current income tax relating to items recognised directly in equity is recognised in equity and not in profit or loss. Management periodically evaluates positions taken in the tax returns with respect to situations in which applicable tax regulations are subject to interpretation and establishes provisions where appropriate.

Deferred taxes

Deferred income tax is provided on all temporary differences at the reporting date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred income tax liabilities are recognised for all taxable temporary differences:

- except where the deferred income tax liability arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, except where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Notes to the Financial Statements

Deferred income tax assets are recognised for all deductible temporary differences, carry-forward of unused tax assets and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry-forward of unused tax assets and unused tax losses can be utilised:

- except where the deferred income tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of deductible temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

The carrying amount of deferred income tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilised. Unrecognised deferred income tax assets are reassessed at each reporting date and are recognised to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the reporting date. Income taxes relating to items recognised directly in equity are recognised in equity and not in the statement of comprehensive income.

Tax consolidation

The Group and its wholly-owned Australian controlled entities have implemented the tax consolidation legislation as of 1 January 2006. Members of the tax consolidated group have entered into a tax funding agreement. Each entity is responsible for remitting its share of the current tax payable (receivable) assumed by the head entity.

In accordance with UIG 1052 and Group accounting policy, the Group has applied the "separate taxpayer within group approach" in which the head entity, Melbourne IT Ltd, and the controlled entities in the tax consolidated group continue to account for their own current and deferred tax amounts.

In addition to its own current and deferred tax amounts, the Group also recognises the current tax liabilities (or assets) and the deferred tax assets arising from unused tax losses and unused tax credits assumed from controlled entities in the tax consolidated group. The allocation of taxes to the head entity is recognised as an increase/ decrease in the controlled entity's inter-company accounts with the tax consolidated Group head entity.

Members of the Group have entered into a tax sharing agreement that provides for the allocation of income tax liabilities between the entities should the head entity default on its tax payment obligations. No amounts have been recognised in the financial statements in respect of this agreement, on the grounds that the possibility is remote.

On 1 May 2015, Uber Global Pty Ltd ('Uber') entered into the tax consolidation Group of Melbourne IT following the acquisition of Uber. On 1 April 2016, InfoReady Pty Ltd ('InfoReady') entered into the tax consolidation Group of Melbourne IT following the acquisition of InfoReady.

Notes to the Financial Statements

Other taxes

Revenues, expenses and assets are recognised net of the amount of GST except:

- where the GST incurred on a purchase of goods and services is not recoverable from the taxation authority, in which case the GST is recognised as part of the cost of acquisition of the asset or as part of the expense item as applicable; and
- receivables and payables are stated with the amount of GST included.

The net amount of GST recoverable from, or payable to, the taxation authority is included as part of receivables or payables in the statement of financial position.

Cash flows are included in the Statement of Cash Flows on a gross basis and the GST component of cash flows arising from investing and financing activities, which is recoverable from, or payable to, the taxation authority are classified as operating cash flows.

Key judgement and estimates

The Group's accounting policy for taxation requires Management's judgement in assessing whether deferred tax assets and certain deferred tax liabilities are recognised in the statement of financial position. Deferred tax assets are recognised only when it is considered more likely than not that they will be recovered, which is dependent on the generation of sufficient future taxable profits.

A4. Dividends

	2016 $'000	2015 $'000
(a) Dividends paid during the year		
Interim franked dividends for 2016: 2.0 cents per share (2015: 1.0 cent per share)	2,015	929
Final franked dividends for 2015: 4.0 cents per share (2014: 4.0 cents per share)	4,017	3,718
Total dividends paid during the year	6,032	4,647
(b) Dividends proposed and not recognised as a liability		
Final franked dividend for the year ended 31 December 2016:		
6.0 cents per share (2015: 4.0 cents per share)	6,052	3,718
(c) Franking credit balance		
The amount of franking credits available for the subsequent financial year are:		
- franking account balance as at the end of the financial year at 30% (2015: 30%)	158	76

Notes to the Financial Statements

A5. Earnings per share

	2016 Cents	2015 Cents
Basic earnings per share	10.86	6.04
Diluted earnings per share	10.67	5.95

The following reflects the income and share data used in the calculations of basic and diluted earnings per share:

	2016 $'000	2015 $'000
Profit for the year attributable to members of the parent	10,727	5,610
	Number of shares	
Weighted average number of ordinary shares used in the calculation of basic earnings per share	98,819,025	92,944,392
Effect of dilution:		
Share options/rights	1,705,684	1,388,914
Adjusted weighted average number of ordinary shares used in calculating diluted earnings per share	100,524,709	94,333,306

Basic earnings per share is calculated as profit for the year attributable to members of the parent, divided by the weighted average number of ordinary shares.

Diluted earnings per share are calculated as profit for the year attributable to members of the parent, divided by the weighted average number of ordinary shares and the dilutive potential ordinary shares.

Performance rights granted to employees are considered to be potential ordinary shares and have been included in the determination of diluted earnings per share to the extent that they are dilutive. These performance rights have not been included in the determination of basic earnings per share.

There have been no transactions involving ordinary shares or potential ordinary shares that would significantly change the number of ordinary shares or potential ordinary shares outstanding between the reporting date and the date of completion of these financial statements.

A6. Segment reporting

Identification of operating segments

An operating segment is a component of an entity that engages in business activities from which it may earn revenues 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 assess its performance and for which discrete financial information is available.

Notes to the Financial Statements

Executive management meet on a monthly basis to assess the performance of each segment by analysing the segment's earnings before interest, tax, depreciation and amortisation ('EBITDA').

Transfer prices between operating segments are set on an arms’ length basis in a manner similar to transactions with third parties. Segment revenue, expense and segment result include transfers between business segments. Those transfers are eliminated on consolidation.

Operating segments have been identified based on the information provided to the Chief Operating Decision Maker, being the CEO. Consistent with the requirements of AASB 8 *Operating Segments*, as the Chief Operating Decision Maker does not receive information regarding segment assets, no disclosure of segment assets has been provided.

The operating segments are identified by Management based on the nature of the customer segment, and the identity of the service line manager. Discrete financial information about each of these operating businesses is reported to the executive management team on at least a monthly basis.

Where operating segments meet the aggregation criteria, these are aggregated into reported segments. Operating segments are aggregated based on similar products and services provided to same type of customers using the same distribution method. The Group's reportable segments are as described below:

Small Medium Business (SMB Solutions)

SMB Solutions provides domain name registrations and renewals, website and email hosting, website development, search engine optimisation and analysis for businesses in Australia and New Zealand.

Enterprise Services (ES)

Enterprise Services provides services including cloud, mobile application development, data and analytics to Australian enterprise and government organisations.

	2016 $’000	2015 $’000
Reconciliation of revenue		
Segment revenue	168,169	149,994
Interest revenue	267	262
Total revenue	**168,436**	**150,256**

Notes to the Financial Statements

The following tables present the revenue and profit information regarding business unit segments for the years ended 31 December 2016 and 31 December 2015.

Year ended 31 December 2016	SMB Solutions $'000	ES $'000	Total $'000
Segment revenue			
Revenue from operating activities			
Registration revenue	44,916	-	**44,916**
Solutions, hosting & services	52,892	70,361	**123,253**
Total segment revenue	**97,808**	**70,361**	**168,169**
Result			
Segment results	15,703	14,644	**30,347**
Unallocated expenses:			
- Corporate (including transaction costs relating to acquisition)			(6,263)
- Gain on sale of IDNR business, net of transaction costs			2,350
- Other income			1,610
- Fair value movement in embedded derivatives			(59)
- Loss on conversion of Tiger Pistol convertible notes			(325)
- Gain on AFS asset			546
Earnings before interest and tax & amortisation			**28,206**
Net Interest			
Interest revenue			267
Interest expense on debt and borrowings			(1,157)
Unwinding of discount on other financial liabilities			(504)
Total Net Interest			(1,394)
Income tax expense			(7,049)
Depreciation & amortisation			(7,055)
Profit after tax for the year			**12,708**

Notes to the Financial Statements

Year ended 31 December 2015	SMB Solutions	ES	Total
	$'000	$'000	$'000
Segment revenue			
Revenue from operating activities			
Registration revenue	55,932	-	**55,932**
Solutions, hosting & services	53,294	40,746	**94,040**
Other revenue	22	-	**22**
Total segment revenue	**109,248**	**40,746**	**149,994**
Result			
Segment results	16,324	7,554	**23,878**
Unallocated expenses:			
- Corporate (including transaction costs relating to Uber and Outware acquisitions)			(7,368)
Earnings before interest and tax & amortisation			**16,510**
Net Interest			
Interest revenue			262
Interest expense on debt and borrowings			(744)
Unwinding of discount on other financial liabilities			(467)
Total Net Interest			**(949)**
Income tax expense			(3,257)
Depreciation & amortisation			(5,576)
Profit after tax for the year			**6,728**

A7. Gain on sale of International Domain Name Registration (IDNR) business

On 31 March 2016, Melbourne IT completed the sale of its International Domain Name Registration (IDNR) business for a sale consideration of US$6,000,000 (equivalent to AU$7,800,000). The gain on sale of AUD$2,350,000 includes transaction costs incurred relating to the sale, a portion of goodwill relating to the IDNR business and assets and liabilities relating to the IDNR business.

A8. Other income

	2016	2015
	$'000	$'000
Gain on reassessment of non-controlling interests dividend liability	586	-
Gain on reassessment of contingent consideration liability	1,024	-
Total other income	**1,610**	**-**

Notes to the Financial Statements

Section B: Operating assets and liabilities

B1. Trade and other receivables

	2016 $’000	2015 $’000
Trade receivables	18,929	13,335
Allowance for doubtful debts	(836)	(1,076)
Total trade and other receivables	**18,093**	**12,259**

Trade receivables, which generally have 14-60 day terms, are recognised and carried at amortised cost which is at original invoice amount less an allowance for any uncollectible amounts. An estimate for doubtful debts is made when collection of the full amount is no longer probable. Bad debts are written off when identified.

	2016 $’000	2015 $’000
Opening balance	1,076	1,034
Additional provision / (released)	(231)	139
Amount written off	(9)	(150)
Acquisitions	-	53
Closing balance	**836**	**1,076**

At 31 December, the ageing analysis of trade receivables is as follows:

	2016		2015	
	Gross $’000	Allowance $’000	Gross $’000	Allowance $’000
Consolidated				
Current	11,718	-	6,255	-
0 - 30 days past due	4,021	-	3,430	-
31 – 60 days past due	1,070	-	1,349	-
Past due 61 days +	2,120	(836)	2,301	(1,076)
Closing balance	**18,929**	**(836)**	**13,335**	**(1,076)**

Receivables past due but not considered impaired are $6,375,000 (2015: $6,004,000), and comprise balances owed from customers who have a good history of repayments or are otherwise considered recoverable.

Due to the short-term nature of these receivables, their carrying value is assumed to approximate their fair value. The maximum exposure to credit risk is the fair value of receivables. Collateral is not held as security.

Notes to the Financial Statements

B2. Plant and equipment

	Leasehold improvements $'000	Plant and equipment $'000	Furniture and fittings $'000	Capital work in progress $'000	Total $'000
At cost					
At 1 January 2015	718	8,949	208	958	10,833
Acquisitions of Uber & Outware (note D1)	-	1,915	10	-	1,925
Additions	280	3,231	92	152	3,755
Transfers	173	738	47	(958)	-
At 31 December 2015	**1,171**	**14,833**	**357**	**152**	**16,513**
Acquisition of InfoReady (note D1)	-	44	-	-	44
Additions	426	2,371	-	9	2,806
Transfers	89	63	-	(152)	-
At 31 December 2016	**1,686**	**17,311**	**357**	**9**	**19,363**
Depreciation and impairment					
At 1 January 2015	459	5,363	102	-	5,924
Depreciation charge for the year	127	3,000	36	-	3,163
At 31 December 2015	**586**	**8,363**	**138**	**-**	**9,087**
Depreciation charge for the year	236	3,250	51	-	3,537
At 31 December 2016	**822**	**11,613**	**189**	**-**	**12,624**
Net book value					
At 31 December 2015	**585**	**6,470**	**219**	**152**	**7,426**
At 31 December 2016	**864**	**5,698**	**168**	**9**	**6,739**

Plant and equipment is stated at cost less accumulated depreciation and any impairment in value.

Depreciation is provided on a straight-line or diminishing value basis on all plant and equipment. Major depreciation periods are:

	2016	2015
Leasehold improvements	The lease term	The lease term
Plant and equipment	2 to 4 years	2 to 4 years
Furniture and fittings	2 to 5 years	2 to 5 years

An item of plant and equipment is derecognised upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising from the derecognition of the asset (calculated as the difference between net disposal proceeds and the carrying amount of the asset) is included in the statement of comprehensive income upon derecognition.

Notes to the Financial Statements

The residual values, useful lives and methods of depreciation of plant and equipment are reviewed at each financial year end and adjusted prospectively, if appropriate.

B3. Intangible assets

	2016 $'000	2015 $'000
Goodwill	199,835	182,000
Market related intangibles	9,052	9,052
Accumulated amortisation	(35)	-
	9,017	9,052
Customer contracts	7,977	7,244
Accumulated amortisation	(3,305)	(1,757)
	4,672	5,487
Capitalised software	13,239	11,049
Accumulated amortisation	(4,727)	(2,783)
	8,512	8,266
Other intangibles	315	315
Accumulated amortisation	(315)	(315)
	-	-
Total intangible assets	**222,036**	**204,805**

Goodwill

Goodwill on acquisition is initially measured at cost being the excess of the cost of the business combination over the acquirer's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities.

Following initial recognition, goodwill is measured at cost less any accumulated impairment losses. Goodwill is not amortised. Goodwill is reviewed for impairment, annually or more frequently if events or changes in circumstances indicate that the carrying value may be impaired.

As at the acquisition date, any goodwill acquired is allocated to each of the cash-generating units (CGUs) expected to benefit from the combination's synergies. Goodwill has been allocated, for impairment purposes, to CGUs that are significant individually or in aggregate, taking into consideration the nature of services, resource allocation, how operations are monitored and where independent cash flows are identifiable.

Notes to the Financial Statements

Intangible assets acquired both separately and from a business combination

Intangible assets acquired separately are capitalised at cost and from a business combination are capitalised at fair value as at the date of acquisition. Following initial recognition, the cost model is applied to the class of intangible assets. Where amortisation is charged on assets with finite lives, this expense is taken to profit and loss through the ‘amortisation of identifiable intangible assets’ line item.

Gains or losses arising from derecognition of an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset and are recognised in the profit and loss when the asset is derecognised.

Internally generated intangible assets

Costs relating to the research phase of the project are expensed while costs relating to the development phase are capitalised as Capitalised Software. The costs capitalised are being amortised over a useful life of 4-6 years.

A summary of the policies applied to the Group’s intangible assets is as follows:

Customer Contracts	
Useful lives	Finite
Amortisation	Amortised over the estimated churn of the customer base.
Impairment testing	Amortisation method reviewed annually and when indicators exist.

Market Related Intangibles	
Useful lives	Indefinite
Amortisation	No amortisation.
Impairment testing	Annually and more frequently when indicator exists.

Capitalised Software Projects	
Useful lives	Finite
Amortisation	Amortised over expected useful life of 4-6 years
Impairment testing	Amortisation method reviewed annually and when indicators exist.

The carrying value of any intangible assets denominated in foreign currencies is revalued at the year end spot rate of each reporting period, leading to changes in the carrying value of the intangible assets in reporting currency. Any revaluation amounts are recognised directly in the foreign currency translation reserve.

Impairment of assets

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

Notes to the Financial Statements

The carrying values of assets are reviewed for impairment when events or changes in circumstances indicate the carrying value may not be recoverable. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs. If any such indication exists and where the carrying values exceed the estimated recoverable amount, the assets or cash-generating units are written down to their recoverable amount.

Recoverable amount is the greater of fair value less costs to sell and value in use. It is determined for an individual asset, unless the asset's value in use cannot be estimated to be close to its fair value less costs to sell and it does not generate cash inflows that are largely independent of those from other assets or groups of assets, in which case, the recoverable amount is determined for the CGU to which the asset belongs.

In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

(a) Reconciliation of carrying amounts at the beginning and end of the period

	Capitalised Software $'000	Customer Contracts $'000	Market Related Intangibles $'000	Goodwill $'000	Total $'000
Net balance at 1 January 2015	8,224	1,632	9,052	99,976	118,884
Acquisitions of Uber & Outware (note D1)	-	4,283	-	82,024	86,307
Additions	1,649	378	-	-	2,027
Amortisation	(1,607)	(806)	-	-	(2,413)
Net balance at 31 December 2015	**8,266**	**5,487**	**9,052**	**182,000**	**204,805**
Acquisition of InfoReady (note D1)	-	847	-	23,565	24,412
Additions	2,181	-	-	-	2,181
Disposal	-	(114)	-	(5,730)	(5,844)
Amortisation	(1,935)	(1,548)	(35)	-	(3,518)
Net balance at 31 December 2016	**8,512**	**4,672**	**9,017**	**199,835**	**222,036**

(b) Market related intangibles

Marketing related intangibles represent brand names of past acquisitions. They have been assessed as having indefinite useful lives as they are expected to contribute to future economic benefits indefinitely as Melbourne IT continues to sell its products under these brand names indefinitely and therefore invests in these brands through its marketing activities. Current year amortisation represents the retirement of a brand name.

Notes to the Financial Statements

(c) Customer contracts

Following the acquisition of InfoReady Pty Ltd ('InfoReady') during the year, customer contracts amounting to $847,000 were recognised based on an external valuation. Following the acquisitions of Uber Global Pty Ltd ('Uber') and Outware Systems Pty Ltd ('Outware') during the prior year, customer contracts amounting to $1,145,000 relating to Uber and $3,138,000 relating to Outware were recognised based on the external valuation. The customer contracts are amortised over the period of 5 years based on the historical attrition rate.

(d) Capitalised software

Included in capitalised software were software acquired from Netregistry Pty Ltd (carrying value of $4,550,000) and Oracle Financials, the common financial reporting system used by all entities in the Group with a carrying value of $542,000.

(e) Goodwill and other intangible assets impairment testing

Carrying amount of intangible assets allocated to each of the CGUs:

	SMB Solutions		ES		Total	
	2016	2015	2016	2015	2016	2015
	$'000	$'000	$'000	$'000	$'000	$'000
Goodwill	97,935	103,666	101,900	78,334	199,835	182,000
Market related intangibles	7,734	7,769	1,283	1,283	9,017	9,052
Customer contracts	1,781	2,470	2,891	3,017	4,672	5,487
Capitalised software	7,018	6,200	1,494	2,066	8,512	8,266

Under the impairment testing the carrying amount of each CGU is compared to its recoverable amount. The recoverable amount of each CGU is determined based on a value in use calculation for each CGU to which goodwill and other intangible assets has been allocated.

Key assumptions used in value in use ('VIU') calculations

	SMB Solutions	ES
Growth rate year 2-5(1)	2.50%	2.50%(3)
Growth rate after year 5(2)	2.50%	2.50%
Discount rate(4)	11.21%	11.21%

(1) All value in use calculations are based on management's estimates of achievable EBITDA for the respective CGUs, with growth rates as noted in the table applied to years 2-5. These estimates are most sensitive to assumptions around revenue growth, in particular the timescale for implementation of new products and initiatives in the SMB business. Year 1 results are based on Board approved budgets.

(2) Cash flows beyond the five year period are extrapolated using a 2.5% growth rate (2015: 2.5%) to determine terminal value, which is the Company's estimate of the long term average growth rate for the industry in which the Company operates.

Notes to the Financial Statements

(3) ES CGU's year two growth rate is expected to be greater than 2.5% as a result of the ES CGU continuing its cloud solutions expansion strategy and continued leverage of revenue synergies with InfoReady and Outware. However, for the purposes of determining the VIU of the ES CGU, the long term growth rate of the Group has been adopted.

(4) The discount rate used reflects risks specific to the Group and its operating segments and is derived from its weighted average cost of capital. Segment-specific risk is incorporated by applying individual beta which is assessed annually based on publicly available data.

Results of impairment test and impact of reasonably possible changes in key assumptions

There was no requirement to impair goodwill as a result of the impairment testing. For each CGU the recoverable amount exceeds its carrying amount. As impairment testing is based on assumptions and judgements, the Group has considered changes in key assumptions that they believe to be reasonably possible. For all CGUs, the recoverable amount exceeds the carrying amount when testing for reasonably possible changes in key assumptions.

If all assumptions remain the same, the base year EBITDA would need to decline from the current expected EBITDA by 22% for the SMB CGU and 19% for the ES CGU for the recoverable amounts of the CGUs to equal their carrying values respectively.

Key judgement and estimates

The Group determines whether goodwill and intangibles with indefinite useful lives are impaired at least on an annual basis. This requires an estimation of the recoverable amount of the cash-generating unit, using a value in use discounted cashflow methodology, to which the goodwill and intangibles, with indefinite useful lives are allocated. Key assumptions requiring judgement include projected cashflows based on forecast EBITDA, growth rate estimates and discount rates.

B4. Non-current financial assets

	2016 $'000	2015 $'000
Available for sale financial assets		
Convertible note receivable - 20 October 2014 (a)	-	1,748
Convertible note receivable - 20 November 2015 (b)	-	247
Investment in Tiger Pistol - ordinary shares (c)	1,795	-
	1,795	**1,995**

Convertible notes are accounted for as an Available for Sale debt instrument with an embedded derivative and are recorded at fair value at each reporting date in accordance with AASB *139 Financial Instruments: Recognition and Measurement*. Movements in the fair value of any embedded derivatives are recognised in profit or loss. Imputed interest income on the notes are calculated using the effective interest rate method and recorded in the profit or loss. Movement in the fair value of the non-derivative component of the notes are recognised in Other Comprehensive Income and recorded in the Available-for-sale (AFS) reserve.

In the current year, the Group has changed it's accounting for its investment in convertible notes. In prior periods changes in fair value of the convertible notes were recognised in Other Comprehensive Income and recorded in the AFS reserve.In the

Notes to the Financial Statements

current period the convertible notes have been accounted for as debt instruments (Available for Sale) with an embedded equity call option recognised at fair value through profit or loss. In accordance with Accounting Standards the comparative financial information for the financial year ended 31 December 2015 has not been restated on the basis that the impact of the change in accounting is immaterial to the financial report. If the comparative financial information were restated for this change in accounting, the operating profit before tax would have been increased by approximately $510,000 and the gain recognised in Other Comprehensive Income (AFS reserve) would have been reduced by approximately $452,000.

(a) The Group entered into a Convertible Note Agreement ("Agreement") with Tiger Pistol Pty Ltd (Tiger Pistol) on 20 October 2014. The convertible note contains an embedded derivative and a loan receivable component. The convertible note receivable has a maturity of 5 years from 20 October 2014 (issue date). Coupon rate of 6% per annum will be calculated and payable in arrears or on conversion or redemption of the note, 2 years after the issue date. This financial asset may be converted into 500,000 ordinary shares upon maturity or earlier subject to satisfaction of early redemption or conversion conditions as stipulated in the Agreement.

(b) The Group entered into a second Convertible Note Agreement ("Agreement") with Tiger Pistol on 20 November 2015 pursuant to the recent capital raising exercise. The convertible note contains an embedded derivative and a loan receivable component. The maturity date of the convertible note receivable is 1 February 2018. Upon maturity, or earlier subject to satisfaction of early redemption or conversion conditions as stipulated in the Agreement, this financial asset may be converted into a minimum of 103,205 ordinary shares with the final number of shares dependant on conditions stipulated in the Agreement.

(c) In accordance with the respective convertible note agreements, the Group elected to exercise both convertible note receivable assets to equity in Tiger Pistol on 12 December 2016 for the convertible note maturing in 20 October 2019 ("CN1") and 22 December 2016 for the convertible note maturing on 20 November 2018 ("CN2") respectively. Upon conversion of CN1 and CN2, the Group received 500,000 and 103,205 shares respectively in Tiger Pistol. These shares have been accounted for as a financial asset (Available for Sale), and valued by reference to the most recent arms length transaction of Tiger Pistol shares.

Key judgement and estimates

The fair values of the embedded derivatives on the convertible note receivables are determined using the 'Black Scholes' option pricing model. The key assumption requiring judgement was the calculation of the volatility of Tiger Pistol's shares by reference to comparable companies. The fair value of the non-derivative component of the convertible note receivables are determined using the effective interest rate method.

B5. Trade and other payables

	2016 $'000	2015 $'000
Trade creditors	5,449	3,408
Sundry creditors	3,959	3,109
Deposits received in advance	1,549	2,412
Accrued expenses	7,847	8,148
Total trade and other payables	**18,804**	**17,077**

Notes to the Financial Statements

Trade and other payables are carried at cost and due to their short term nature they are not discounted, therefore their carrying value is assumed to approximate their fair value. They represent liabilities for goods and services provided to the Group prior to the end of the year that are unpaid and arise when the Group becomes obliged to make future payments in respect of the purchase of these goods and services.

Terms and conditions relating to trade and sundry creditors:

(i) Trade creditors are non-interest bearing and are normally settled within agreed trading terms.

(ii) Sundry creditors are non-interest bearing and are normally settled within agreed trading terms.

B6. Provisions

	2016 $'000	2015 $'000
Current		
Employee benefits	3,291	3,151
Other	170	170
	3,461	3,321
Non current		
Employee benefits	803	546
	803	546
Total provisions	**4,264**	**3,867**

The aggregate employee benefit liability comprises:

Provisions (current)	3,291	3,151
Provisions (non current)	803	546

Employee benefits

Provision is made for employee benefits accumulated as a result of employees rendering services up to the reporting date. These benefits include wages and salaries, annual leave and long service leave.

Liabilities arising in respect of wages and salaries, annual leave and any other employee benefits expected to be settled within twelve months of the reporting date are measured at their nominal amounts based on remuneration rates which are expected to be paid when the liability is settled. All other employee benefit liabilities are measured at the present value of the estimated future cash outflow to be made in respect of services provided by employees up to the reporting date. In determining the present value of future cash outflows, the market yield as at the reporting date on corporate bonds, which have terms to maturity approximating the terms of the related liability are used.

Employee benefit expenses arise in respect of the following categories:

- wages and salaries, non-monetary benefits, annual leave, long service leave and other entitlements; and
- other types of employee entitlements are recognised against profits on a net basis in their respective categories.

Other provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

Notes to the Financial Statements

Section C: Capital and financial risk management

C1. Financial risk management objectives and policies

The Group's principal financial instruments comprise of receivables, payables, interest bearing loans, cash, short-term deposits, derivatives, non-current financial asset and other financial liabilities. The Group manages its exposure to key financial risks in accordance with the Group's financial risk management policy. The objective of the policy is to support the delivery of the Group's financial targets whilst protecting financial security.

The purpose is to manage the financial risks arising from the Group's operations. The main risks arising from the Group's financial instruments are interest rate risk, foreign currency risk, liquidity risk and credit risk. The Group uses different methods to measure and manage different types of risks to which it is exposed. These include monitoring levels of exposure to foreign exchange risk and interest rate risk, assessments of market forecasts for foreign exchange and interest rate. Liquidity risk is monitored through the development of rolling cash flow forecasts.

The Board reviews and agrees policies for managing each of these risks as summarised below. Primary responsibility for identification and control of financial risks rests with Management under the supervision of the Audit and Risk Management Committee and under the authority of the Board. The Board reviews and agrees policies for managing each of the risks identified below, including the setting of limits for trading in derivatives, hedging cover of foreign currency and interest rate risk, credit allowances, and cash flow forecast projections.

Capital management

For the purpose of the Group's capital management, capital includes issued capital, and all other equity reserves attributable to the equity holders of the parent. When managing capital, the Board's objective is to ensure the entity continues as a going concern as well as to maintain optimal returns to shareholders and benefits for other stakeholders.

The Group manages its capital structure and makes adjustments in light of changes in economic conditions and requirements of the financial covenants. To maintain or adjust the capital structure, the Group may adjust the dividend payment to shareholders, return capital to shareholders, issue new shares or sell assets to reduce debt.

During 2016, the Group paid dividends of $6,032,000 (2015: $4,647,000).

On 22 February 2017, the directors declared a final dividend amounting to $6,052,000. On 23 February 2016, the directors declared a final dividend amounting to $3,718,000.

Risk exposures and responses

Interest rate risk

The Group's exposure to market interest rates related primarily to the Group's short term deposits held and drawdowns on available financing facilities. Refer to Note C4 for details of available financing facilities.

At balance date, the Group had the following mix of financial assets and liabilities exposed to variable interest rate risk.

Notes to the Financial Statements

	2016 $'000	2015 $'000
Financial assets		
Cash and cash equivalents	16,426	12,370
Financial Liabilities		
Bank loan[1]	36,500	30,000
Finance leases	128	342

(1) Of the financial assets and liabilities that are exposed to variable interest rates, $20,300,000 of bank loans drawn are covered by interest rate swap agreements as at 31 December 2016. Refer to note C7(b) for further detail.

The following sensitivity analysis is based on the interest rate risk exposures in existence at the reporting date.

At 31 December 2016 and 2015, if interest rates had moved, as illustrated in the table below, with all other variables held constant, post tax profit and equity would have been affected as follows:

	Net Profit Higher / (Lower)		Equity Higher / (Lower)	
	2016 $'000	2015 $'000	2016 $'000	2015 $'000
Consolidated				
Assets + 0.25% (25 basis points), , Liabilities + 0.25% (25 basis points) Liabilities (no change), (2015: Assets + 0.25% (25 basis points)).	-	(5)	-	(5)
Assets - 0.25% (25 basis points), Liabilities - 0.25% (25 basis points) Liabilities (no change), (2015: Assets - 0.25% (25 basis points)).	-	5	-	5

The sensitivities have been calculated based on average holdings of interest bearing assets and liabilities restated at year end exchange rates. Interest bearing assets are predominantly sensitive to movements in Australian interest rates.

Credit risk

Credit risk arises from the financial assets of the Group, which comprise cash and cash equivalents, trade and other receivables, and derivative instruments. The Group's exposure to credit risk arises from potential default of the counter party, with a maximum exposure equal to the carrying amount of these instruments. Exposure at balance date is addressed in each applicable note.

The Group provides credit only with recognised, creditworthy third parties, and as such collateral is not required nor is it the Group's policy to securitise its trade and other receivables.

It is the Group's policy that all customers who wish to trade on credit terms are subject to credit verification procedures which may include an assessment of their financial position, past experience and industry reputation, depending on the amount of credit to be granted. In addition, receivable balances are monitored on an ongoing basis.

Notes to the Financial Statements

Foreign currency risk

The Group conducts some amount of its business in US dollars ('USD') and is therefore exposed to movements in the AUD/USD dollar exchange rate. The Group actively manages the gross margin risk by its foreign currency risk management strategy. Please refer to Note C7 for further details.

Both the functional and presentation currency of Melbourne IT Ltd is in Australian dollars (AUD). The consolidated Group contains functional currencies in USD and NZD. Transactions in foreign currencies are initially recorded in the functional currency at the exchange rates ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the rate of exchange ruling at the reporting date.

The exchange differences arising on the retranslation are taken directly to other comprehensive income. On disposal of a foreign entity, the deferred cumulative amount recognised in other comprehensive income relating to that particular foreign operation is recognised in the determination of profit and loss for the year.

At 31 December 2016, the Group had the following exposures to USD denominated assets and liabilities, where the functional currency is not USD. The Group's exposure to foreign currency changes for all other currencies is not material. Assets and liabilities that are designated in cashflow hedges are not included:

	2016 $'000	2015 $'000
Financial Assets		
Cash and cash equivalents	1,750	1,650
Trade and other receivables	207	198
	1,957	**1,848**
Financial Liabilities		
Trade and other payables	(773)	(1,725)
Net exposure	**1,184**	**123**

The following sensitivity is based on foreign currency risk exposures in existence at the reporting date.

At 31 December 2016, had the Australian Dollar moved, as illustrated in the table below, with all other variables held constant, post tax profit and equity would have been affected as follows:

	Net Profit Higher / (Lower)		Equity Higher / (Lower)	
	2016 $'000	2015 $'000	2016 $'000	2015 $'000
Consolidated				
- AUD/USD +10% (2015: +1%)	(105)	(1)	(105)	(1)
- AUD/USD -10% (2015: -10%)	128	14	128	14

Notes to the Financial Statements

The Group also has exposures to foreign exchange when retranslating foreign currency subsidiaries into Australian Dollars. The sensitivity range has been determined using an expected range of 0.647 to 0.791 USD/AUD for the retranslation of USD denominated balances for the forthcoming year.

Liquidity risk

Liquidity risk is managed via the regular review of forecasted cash inflows and outflows, with any surplus funds being placed in short term deposits to maximise interest revenue.

The risk implied from the values shown in the table below, reflects a balanced view of cash inflows and outflows. Trade payables and other financial liabilities mainly originate from the financing of assets used in ongoing operations such as plant, equipment and investments in working capital (e.g. trade receivables). These assets are considered in the Group's overall liquidity risk. To monitor existing financial assets and liabilities as well as to enable an effective controlling of future risks, the Company has established comprehensive risk reporting covering its business units that reflects expectations of settlement of financial assets and liabilities. The amounts disclosed in the table are the contractual undiscounted cash flows.

Notes to the Financial Statements

	< 6 Months $'000	6 - 12 Months $'000	1 to 5 Years $'000	> 5 Years $'000	Total $'000
31 December 2016					
Financial assets					
Cash and cash equivalents	16,426	-	-	-	16,426
Trade and other receivables	18,093	-	-	-	18,093
Other financial assets	-	-	1,795	-	1,795
	34,519	-	1,795	-	36,314
Financial liabilities					
Trade and other payables	(18,804)	-	-	-	(18,804)
Borrowings	(54)	(44)	(36,537)	-	(36,635)
Other financial liabilities	(1,261)	(29,828)	(8,315)	-	(39,404)
	(20,119)	(29,872)	(44,852)	-	(94,843)
Net inflow/(outflow)	**14,400**	**(29,872)**	**(43,057)**	**-**	**(58,529)**
31 December 2015					
Financial assets					
Cash and cash equivalents	12,370	-	-	-	12,370
Trade and other receivables	12,259	-	-	-	12,259
Other financial assets	-	-	1,995	-	1,995
	24,629	-	1,995	-	26,624
Financial liabilities					
Trade and other payables	(17,077)	-	-	-	(17,077)
Borrowings	(119)	(106)	(30,151)	-	(30,376)
Other financial liabilities	-	(18,885)	(27,274)	-	(46,159)
	(17,196)	(18,991)	(57,425)	-	(93,612)
Net inflow/(outflow)	**7,433**	**(18,991)**	**(55,430)**	**-**	**(66,988)**

Notes to the Financial Statements

C2. Contributed equity

	2016 $'000	2015 $'000
(a) Issued and paid-up capital		
Ordinary shares each fully paid	51,026	35,629

(b) Movements in shares on issue

	2016 Number of shares	2016 $'000	2015 Number of shares	2015 $'000
Beginning of the financial year	92,944,392	35,629	92,944,392	35,629
Issued during the year:				
- Capital raising	7,500,000	15,000	-	-
- Dividend reinvestment plan	416,938	821	-	-
- Transaction costs for capital raising, net of tax	-	(424)	-	-
End of the financial year	**100,861,330**	**51,026**	**92,944,392**	**35,629**

Ordinary share capital is recognised at the fair value of the consideration received by the Company. Any transaction costs arising on the issue of ordinary shares are recognised directly in equity as a reduction of the share proceeds received.

The ordinary shares have no par value in accordance with *Corporations Act 2001*.

C3. Reserves

	2016 $'000	2015 $'000
Options reserve	1,398	776
Foreign currency translation reserve	(593)	(573)
Hedging reserve	3	(82)
Other reserves	8,523	3,646
Available-for-sale (AFS) reserve	-	498
	9,331	**4,265**

Notes to the Financial Statements

Options reserve

The options reserve is used to recognise the value of equity-settled share based payment transactions provided to employees, including Key Management Personnel, as part of their remuneration. Refer to Note E6 for further details of these plans.

Foreign currency translation reserve

The foreign currency translation reserve is used to record exchange differences arising from the translation of the financial statements of foreign subsidiaries.

Hedging reserve

The hedge reserve contains the effective portion of the hedge relationships incurred as at the reporting date.

Other reserve

Other reserve is used to record the difference between derecognition of the non-controlling interests and recognition of the financial liabilities.

Available-for-sale (AFS) reserve

A change to the fair value of the non-derivative component of the non-current financial asset was recorded against the available-for-sale reserve. Refer to note B4 for further details.

C4. Borrowings

	2016 $'000	2015 $'000
Current		
Finance lease liabilities	92	198
Finance lease liabilities	92	198
Non current		
Finance lease liabilities	36	144
Interest bearing loan	36,500	30,000
	36,536	30,144

Notes to the Financial Statements

Interest-bearing loans and borrowing costs

All loans and borrowings are initially recognised at the fair value of the consideration received less directly attributable transaction costs. After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortised cost using the effective interest method. Fees paid on the establishment of loan facilities that are yield related are included as part of the carrying amount of the loans and borrowings. Borrowings are classified as current liabilities unless the group has an unconditional right to defer settlement of the liability for a least 12 months after the reporting date.

The facility is secured via a negative pledge plus a mortgage over shares in Outware Systems Pty Ltd, which is released once 100% ownership taken and Outware Systems Pty Ltd accedes to facility agreement (following whitewash approval by shareholders).

Borrowing costs are recognised as an expense when incurred. Borrowing costs consist of interest and other costs that an entity incurs in connection with the borrowing of funds.

At 30 June 2015, $30,000,000 was drawn down from the ANZ banking facility to fund the acquisition of 50.2% interest in Outware Systems Pty Ltd of which $3,500,000 was used to repay NAB. A further $10,600,000 was drawn down from the ANZ banking facility to fund the acquisition of a further 24.9% interest in Outware Systems Pty Ltd on 31 August 2016. The ANZ bank facility has a maturity date of 1 January 2019. Interest rate is based on the relevant period BBSY rate (which has been between 1.66-2.14% p.a. during the year). The cash advance facility balance is approximate to fair value given that it is an interest bearing loan at floating interest rate. During the year ended 31 December 2016, the Group made loan repayments of $4,100,000.

Leases

The determination of whether an arrangement is, or contains, a lease is based on the substance of the arrangement at the inception date. The arrangement is assessed for whether fulfilment of the arrangement is dependent on the use of a specific asset(s) or the arrangement conveys a right to use the asset(s), even if that right is not explicitly specified in an arrangement.

Leases where the lessor retains substantially all the risks and benefits of ownership of the asset are classified as operating leases. Operating lease payments are recognised as an expense in the profit and loss on a straight-line basis over the lease term. Operating lease incentives are recognised as a liability when received and subsequently reduced by allocating lease payments between rental expense and reduction of the liability.

The Group has entered into finance leases for some items of equipment whereby the present value of the minimum lease payments approximates $128,000 (2015: $342,000). Refer to note C5 for further details.

Notes to the Financial Statements

Financing facilities available

At reporting date, the following financing facilities had been negotiated and were available:

	Total facilities		Facilities used at reporting date	
	2016	2015	2016	2015
	$'000	$'000	$'000	$'000
- Business lending - cash advance facility	83,600	83,600	36,500	30,000
- Business lending - bank guarantees	3,800	3,030	1,803	2,192
- Asset finance - leasing	5,000	5,000	-	-
- Standby letters of credit	3,200	3,200	1,120	2,944
	95,600	94,830	39,423	35,136

C5. Commitments

	2016	2015
	$'000	$'000
Operating lease commitments		
Operating leases		
Minimum lease payments		
- not later than 1 year	2,930	3,085
- later than 1 year and not later than 5 years	7,362	8,436
- later than 5 years	457	1,559
Aggregate lease expenditure contracted for at reporting date	10,749	13,080

Finance lease commitments

The Group has finance leases for various items of plant and machinery. The effective interest rate of these non-cancellable finance leases are between 8.0 - 8.5% p.a. The Group's obligations under finance leases are secured by the lessor's title to the leased assets. Future minimum lease payments under finance leases together with the present value of the net minimum lease payments are as follows:

Notes to the Financial Statements

	2016		2015	
	Minimum payments	Present value of payments	Minimum payments	Present value of payments
	$ '000	$ '000	$ '000	$ '000
Within 1 year	106	99	225	198
After 1 year but not more than 5 years	29	29	151	144
More than 5 years	-	-	-	-
Total minimum lease payments	135	128	376	342
Less amounts representing finance charges	(7)	-	(34)	-
Present value of minimum lease payments	**128**	**128**	**342**	**342**

Financial instruments

The details of hedging instruments held and guarantees issued are as follows:

(a) Hedges of specific commitments

Refer to Note C7 for details of hedging instruments the Group entered into to manage its foreign currency risk exposure.

(b) Financial Guarantees and other credit facilities

The face value of financial guarantees issued by the Group are presented below.

(a) Bank Guarantees of AU$1,803,000 have been issued in favour of various parties in accordance with the Group's property commitments.

(b) The Company has Standby Letters of Credit totalling US$772,000 (equivalent to AU$1,120,000) in accordance with various Registry Licence Agreements.

Notes to the Financial Statements

C6. Other financial liabilities

	2016 $’000	2015 $’000
Current		
Put options liability	29,828	17,030
Dividend liability to non-controlling interests	1,261	1,855
Contingent consideration liability	-	-
	31,089	**18,885**
Non-current		
Put options liability	-	25,953
Dividend liability to non-controlling interests	-	1,321
Contingent consideration liability	8,315	-
	8,315	**27,274**

The other financial liabilities represent the fair value of the put options to acquire the remaining 24.9% interest in Outware Systems Pty Ltd (Outware) (refer to Note D1(c) for more details), estimated dividend liability due to non-controlling interests over the next year (refer to Note D1(c) for more details) and contingent consideration liability in relation to acquisition of InfoReady Pty Ltd (refer to Note D1(a) for more details).

Key judgement and estimates

The fair value of the put options liability has been determined based on actual financial performance of Outware for the 6 months ended 31 December 2016 and forecast financial performance for the period ending 30 June 2017 and on the expected EBITDA multiple that will be paid. The fair value of the put options is reassessed at each reporting date with movements being recorded in an equity reserve.

The dividend liability due to non-controlling interests of Outware (after taking into consideration the dividend paid out during the current financial year) was remeasured at 31 December 2016 based on expected surplus funds of which dividend payments will be made in the next 12 months with the movement recognised in the profit or loss.

The contingent consideration liability was calculated based on the excess of the EBITDA performance during the earnout periods over the EBITDA threshold amount specified in the Sale and Purchase Agreement relating to the acquisition of InfoReady for each of the earnout period multiplied by three.

Notes to the Financial Statements

C7. Derivative financial liabilities/(assets)

	2016 $'000	2015 $'000
Foreign exchange contracts (a)	(155)	17
Interest rate swap (b)	151	100
	(4)	117

The Group conducts some amount of its business in US dollars ('USD') and is therefore exposed to movements in the AUD/USD dollar exchange rate. The Group actively manages this risk via its foreign currency risk management strategy.

The Group uses derivative financial instruments, such as forward currency contracts and interest rate swaps, to hedge its risks associated with currency and interest rate fluctuations. Such derivative financial instruments are stated at fair value. The fair value of forward currency contracts is calculated by reference to current forward exchange rates for contracts with similar maturity profiles.

For the purposes of hedge accounting, hedges are classified as cash flow hedges where they hedge exposure to variability in cash flows that is either attributable to a particular risk associated with a recognised asset or liability or a forecasted transaction. In relation to cash flow hedges (forward foreign currency contracts) to hedge firm commitments that meet the conditions for hedge accounting, the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognised directly in other comprehensive income and the ineffective portion is recognised in the determination of profit and loss for the year.

When the hedged firm commitment results in the recognition of an asset or a liability, then, at the time the asset or liability is recognised, the associated gains or losses that had previously been recognised in other comprehensive income are included in the initial measurement of the acquisition cost or other carrying amount of the asset or liability.

For all other cash flow hedges, the gains or losses that are recognised in other comprehensive income are transferred to profit and loss in the same year in which the hedged firm commitment affects the net profit and loss, for example when the future sale actually occurs.

For derivatives that do not qualify for hedge accounting, any gains or losses arising from changes in fair value are taken directly to profit and loss.

Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated or exercised, or no longer qualifies for hedge accounting. At that point in time, any cumulative gain or loss on the hedging instrument recognised in other comprehensive income is kept in equity until the forecasted transaction occurs. If a hedged transaction is no longer expected to occur, the net cumulative gain or loss recognised in equity is transferred to profit and loss.

(a) Foreign exchange contracts

At 31 December 2016, the Group held six foreign exchange contracts (2015: seven foreign exchange contracts) designated as cash flow hedges of expected net USD cash payments which the Company has firm commitments. The terms of these foreign exchange contracts were negotiated to match the terms of the commitments. The exchange contracts were used to reduce the exposure of foreign exchange risk.

Notes to the Financial Statements

(b) Interest rate swap

At 31 December 2016, the Group held two interest rate swap contracts for $15,000,000 and $5,300,000 designed to hedge the variable interest rate exposure relating to the facility tranches of $30,000,000 and $10,600,000 respectively.

At 31 December 2015, the Group held one interest rate swap contract for $15,000,000 designed to hedge the variable interest rate exposure relating to the facility tranche of $30,000,000.

As at 31 December 2016, an unrealised gain of $85,000 (2015: $113,000 loss) was included in other comprehensive income in respect of these contracts.

C8. Fair value measurement

The Group measures financial instruments such as derivatives at fair value at each reporting date. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either (1) in the principal market for the asset or liability or (2) in the absence of a principal market, in the most advantageous market for the asset or liability. The fair value of an asset or liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that the market participants act in their economic best interest.

All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorised within their fair value hierarchy, described as follows, based on the lowest level of input that is significant to the fair value measurement as a whole:
- Level 1 - Quoted (unadjusted) market prices in active markets for identical assets or liabilities.
- Level 2 - Valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable.
- Level 3 - Valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable.

For assets and liabilities that are recognised in the financial statements at fair value on a recurring basis, the Group determines whether transfers have occurred between levels in the hierarchy by re-assessing categorisation (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

The following table provides the fair value measurement hierarchy of the Group's assets and liabilities.

Notes to the Financial Statements

Fair value measurement hierarchy for assets as at 31 December 2016:

			Fair value measurement using		
	Date of valuation	Total $'000	Quoted prices in active markets (Level 1) $'000	Significant observable inputs (Level 2) $'000	Significant unobservable inputs (Level 3) $'000
Assets/ (liabilities) measured at fair value:					
Derivative financial instruments					
Foreign exchange forward contracts - USD(1)	31 December 2016	155	-	155	-
Interest rate swap(2)	31 December 2016	(151)	-	(151)	-
AFS financial assets					
Investment in Tiger Pistol(3)	31 December 2016	1,795	-	1,795	-
Other financial liabilities					
Put options liability(4)	31 December 2016	(29,828)	-	-	(29,828)
Dividend liability to non-controlling interests(5)	31 December 2016	(1,261)	-	-	(1,261)
Contingent consideration liablity(6)	31 December 2016	(8,315)	-	-	(8,315)
Interest bearing loan(7)	31 December 2016	(36,500)	-	(36,500)	-

(1) Reflects the fair value of foreign exchange contracts, designated as cash flow hedges.

(2) Reflects the fair value of the interest rate swap, designated as a cash flow hedge.

(3) Reflects the fair value by reference to the most recent arms-length transaction of Tiger Pistol shares. Refer to other details disclosed in Note B4.

(4) The fair value of put option liability which entitles Melbourne IT to acquire (and the non-controlling interest to sell) the remaining 24.9% shareholding next year is based on the forecast financial performance (EBITDA) and expected EBITDA multiple as stipulated in the agreement for the financial period ending 30 June 2017, both of which are significant unobservable inputs. The fair value is determined using the discounted cash flow method. Refer to other details disclosed in Notes C6 and D1.

(5) The dividend liability represents the estimated amount to be paid out to non-controlling interests for the financial period ending 30 June 2017 as stipulated in the Shareholders Agreement entered between Melbourne IT and non-controlling shareholders. Refer to other details disclosed in Notes C6 and D1.

(6) The fair value of the contingent consideration liability is estimated based on the estimated excess of the EBITDA performance during the earnout periods over the EBITDA threshold amount specified in the Share Purchase Agreement for each of the earnout period is multiplied by three. A change in the EBTIDA above the threshold will result in a change in the contingent consideration liability of three times that amount. The earnout periods start from 1 April to 31 March the following year until 31 March 2019. Significant unobservable inputs used in the determination of the contingent consideration include forecast EBITDA performance for the first earnout period

Notes to the Financial Statements

(1 April 2016 to 31 March 2017), and revenue and EBITDA growth rates for the second and third earnout periods from the first earnout period. The fair value is determined using the discounted cash flow method. Refer to other details disclosed in Notes C6 and D1.

(7) The carrying value of the interest bearing loan approximate its fair value.

Fair value measurement hierarchy for assets as at 31 December 2015:

			Fair value measurement using		
	Date of valuation	Total $'000	Quoted prices in active markets (Level 1) $'000	Significant observable inputs (Level 2) $'000	Significant unobservable inputs (Level 3) $'000
Assets/ (liabilities) measured at fair value:					
Derivative financial instruments					
Foreign exchange forward contracts - USD	31 December 2015	(17)	-	(17)	-
Interest rate swap	31 December 2015	(100)	-	(100)	-
AFS financial assets					
Convertible note receivable	31 December 2015	1,995	-	1,995	-
Other financial liabilities					
Put options liability	31 December 2015	(42,983)	-	-	(42,983)
Dividend liability to non-controlling interests	31 December 2015	(3,176)	-	-	(3,176)
Interest bearing loan	31 December 2015	(30,000)	-	(30,000)	-

There have been no transfers between Level 1, Level 2 and Level 3 during the period.

Notes to the Financial Statements

Section D: Group structure

D1. Business combinations

Acquisitions in 2016

(a) InfoReady Pty Ltd

On 31 March 2016, Melbourne IT acquired 100% of InfoReady Pty Ltd (InfoReady), a leading data and analytics provider for the Enterprise Services market, for purchase consideration of $15,332,000 (including working capital adjustment) and three earn outs based on annual EBITDA performance for the three years from April 2016 to March 2019. The acquisition was funded through cash. The addition of data analytics capability completed the foundation elements of the Enterprise Services strategy and sits alongside cloud, mobile, security and cloud enabled application development. Melbourne IT's expertise now enables it to deliver complete digital solutions for corporate and government organisations.

Assets acquired and liabilities assumed

The net assets recognised in the 30 June 2016 half year financial report were based on a provisional assessment of their fair value while the Group completed the fair value assessment. The fair values of the identifiable assets and liabilities of InfoReady as at the date of acquisition were:

	Fair value recognised on acquisition		
	Provisional	Adjustments	Final
	$'000s	$'000s	$'000s
Assets			
Trade and other receivables	2,088	-	2,088
Plant and equipment	47	(3)	44
Intangibles	-	847	847
Deferred tax assets	-	171	171
Other assets	85	-	85
	2,220	1,015	3,235
Liabilities			
Trade and other payables	1,333	26	1,359
Provisions	518	-	518
Deferred tax liabilities	-	254	254
	1,851	280	2,131
Total identifiable net liabilities at fair value	369	735	1,104
Goodwill arising on acquisition	24,322	(757)	23,565
Purchase consideration transferred	**24,691**	**(22)**	**24,669**

Notes to the Financial Statements

As at 31 December 2016, the Group has completed the fair value assessment on the net assets acquired. The nature of the changes arising from the fair value assessment are as described below.

- The Group sought an independent valuation for intangibles other than goodwill and $847,000 of customer contracts and relationships were identified. The fair value of the intangibles was determined using the income approach that is multi period excess earnings method.
- The Group carried out an assessment of existing plant and equipment and wrote off those not used at acquisition date.
- The Group carried out an assessment of the trade and other payables and adjusted for those arising at acquisition date. An additional payroll tax liability was identified during this review.
- Changes to deferred tax balances were based on the tax provision calculated at acquisition date and taking into account changes in net assets arising from the fair value assessment.

From the date of acquisition to 31 December 2016, InfoReady has contributed $14,785,000 to the Group's revenue and $1,675,000 to the Group's profit after tax attributable to members of the parent. If the combination had taken place at the beginning of the year, the Group's revenue would have been $172,000,000 and profit after tax attributable to members of the parent would have been $11,143,000.

Purchase consideration	$'000s
Cash paid	15,382
Working capital adjustment	(50)
Contingent consideration liability	9,337
	24,669

Transaction costs of $595,000 were expensed and fully paid. This was included in the cash flows from investing activities.

Contingent consideration liability

As part of the Share Purchase Agreement ('SPA') with the previous owners of InfoReady, three earnout payments have been agreed. The earnout payments are calculated based on the excess of the EBITDA performance during the earnout periods over the EBITDA threshold amount specified in the SPA for each of the earnout period multiplied by three. The earnout periods start from 1 April to 31 March the following year until 31 March 2019. If the EBITDA threshold amount is not achieved during each of the earn out periods, then the minimum contingent consideration payable will be nil. The maximum amount payable is dependent upon the excess of the of the EBITDA performance during the earnout period over the EBITDA threshold amount specified in the SPA for each of the earnout period multiplied by three.

As at acquisition date, the fair value of the contingent consideration was estimated to be $9,337,000 representing the total of the three earnout amounts. Key input assumptions used in the determination of the contingent consideration include forecast EBITDA performance for the first earnout period (1 April 2016 to 31 March 2017), and revenue and EBITDA growth rates for the second and third earnout periods from the first earnout period. The fair value is determined using the discounted cash flow method.

The fair value of the contingent consideration has been remeasured at 31 December 2016 based on forecast EBITDA and the movement recognised in the profit or loss. Significant increase/(decrease) in the EBITDA performance of InfoReady during the earnout periods would result in higher/(lower) fair value of the contingent consideration liability. This contingent consideration liability is categorised as a Level 3 item of the fair value hierarchy.

Notes to the Financial Statements

Acquisitions in 2015

(b) Uber Global Pty Ltd

On 30 April 2015, Melbourne IT acquired 100% of Uber Global Pty Ltd and its controlled entities (Uber), a major domains and hosting services provider, for purchase consideration of $14,909,000 (including working capital adjustment) and an earnout based on EBITDA performance to 30 June 2015. There was no consideration paid on the earn out based on EBITDA performance to 30 June 2015. The acquisition was funded through cash. The combined enlarged group will be able to offer best in class domain names and hosting products and to compete more effectively against strong, price driven, foreign competition.

Assets acquired and liabilities assumed

The net assets recognised in the 30 June 2015 half year financial report were based on a provisional assessment of their fair value while the Group completed the fair value assessment. The fair values of the identifiable assets and liabilities of Uber as at the date of acquisition were:

	Fair value recognised on acquisition		
	Provisional	**Adjustments**	**Final**
	$'000s	**$'000s**	**$'000s**
Assets			
Trade and other receivables	1,153	(433)	720
Plant and equipment	2,253	(495)	1,758
Intangibles	-	1,145	1,145
Deferred tax assets	603	634	1,237
Current tax receivable	-	271	271
Other assets	21	430	451
	4,030	1,552	5,582
Liabilities			
Trade and other payables	2,029	632	2,661
Income received in advance	3,136	593	3,729
Deferred tax liabilities	2,493	(2,147)	346
	7,658	(922)	6,736
Total identifiable net liabilities at fair value	(3,628)	2,474	(1,154)
Goodwill arising on acquisition	18,897	(2,834)	16,063
Purchase consideration transferred (cash paid)	**15,269**	**(360)**	**14,909**

As at 31 December 2015, the Group has completed the fair value assessment on the net assets acquired. The nature of the changes arising from the fair value assessment are as described overleaf.

Notes to the Financial Statements

- The fair value of the trade and other receivables amounts to $720,000, based on an assessment of the recoverability of the receivables at acquisition date. The gross amount of trade and other receivables was $773,000.

- The Group sought an independent valuation for intangibles other than goodwill and $1,145,000 of customer contracts and relationships were identified. The fair value of the intangibles was determined using the income approach that is the multi period excess earnings method.

- The Group carried out an assessment of existing plant and equipment and wrote off those not used at acquisition date.

- Income received in advance and prepayment on domain names registry charges (included in Other assets) were adjusted to follow the Group's accounting policy where performance obligations remain.

- Based on the final tax return of Uber at acquisition date, a tax refund of $270,000 was calculated, resulting in a current tax receivable.

- The Group carried out an assessment of the trade and other payables and adjusted for those arising at acquisition date. This included a supplier claim that was not recorded by Uber at acquisition date of $360,000, which also resulted in the working capital adjustment.

- Changes to deferred tax balances were based on the tax provision calculated at acquisition date and taking into account changes in net assets arising from the fair value assessment.

From the date of acquisition, Uber has contributed $9,628,000 to the revenue and $395,000 to the profit after tax attributable to members of the parent. If the combination had taken place at the beginning of the year, Group revenue would have been $155,138,000 and profit after tax attributable to members of the parent would have been $5,861,000.

The goodwill comprises the fair value of expected synergies and future earnings arising from acquisition.

(c) Outware Systems Pty Ltd

On 16 June 2015, Melbourne IT acquired a 50.2% shareholding of Outware Systems Pty Ltd ('Outware') for $22,722,000 (including working capital adjustment) with put and call options in place to acquire up to 100% of Outware over the next two years. Outware is a leader in the design and development of mobile applications for enterprise and government customers. To facilitate the acquisition, Melbourne IT entered into a cash advance facility with Australia and New Zealand Banking Group Limited ('ANZ') in June 2015. The Outware acquisition is firmly in line with the Group's strategy of building its Enterprise Services into the leading software enabled cloud solutions provider in Australia.

Notes to the Financial Statements

Assets acquired and liabilities assumed

	Fair value recognised on acquisition		
	Provisional	Adjustments	Final
	$'000s	$'000s	$'000s
Assets			
Cash	1,421	-	1,421
Trade and other receivables	3,331	-	3,331
Plant and equipment	167	-	167
Intangibles	-	3,138	3,138
Deferred tax assets	95	216	311
Other assets	507	-	507
	5,521	3,354	8,875
Liabilities			
Trade and other payables	2,072	-	2,072
Current tax liability	329	106	435
Deferred tax liabilities	-	941	941
	2,401	1,047	3,448
Total identifiable net assets at fair value	**3,120**	**2,307**	**5,427**
Non-controlling interests measured at fair value	45,266	-	45,266
Dividend liability to non-controlling interests	3,400	-	3,400
Purchase consideration (including working capital adjustment)	22,722	-	22,722
	71,388	-	71,388
Goodwill arising on acquisition	**68,268**	**(2,307)**	**65,961**

As at 31 December 2015, the Group has completed the fair value assessment on the net assets acquired. The nature of the changes arising from the fair value assessment are as described below.

- The Group sought an independent valuation for intangibles other than goodwill and $3,138,000 of customer contracts and relationships were identified. The fair value of the intangibles was determined using the income approach that is the multi period excess earnings method.

- Changes to current tax liability and deferred tax balances were based on the tax provision estimated at acquisition date and taking into account changes in net assets arising from the fair value assessment.

The fair value and gross amount of the trade and other receivables amounts to $3,331,000.

From the date of acquisition, Outware has contributed $9,987,000 to the revenue and $904,000 to the profit after tax attributable to members of the parent. If the combination had taken place at the beginning of the year, Group revenue would have been $158,056,000 and profit after tax attributable to members of the parent would have been $6,537,000.

Notes to the Financial Statements

The goodwill comprises the fair value of future earnings arising from acquisition.

2016 transactions relating to Outware

On 31 August 2016, the Group exercised its option to purchase 24.9% of share capital in Outware for a cash consideration of $10,622,000.

The minimum and maximum EBITDA multiple payable is 3.75 times and 15.75 times, respectively. The face value of the put/call options liability has been reassessed at 31 December 2016 to be $29,239,000 reflecting the option to purchase the remaining 24.9% non-controlling interest in Outware, bringing the estimated total consideration to be approximately $61,162,000 (net of cash acquired), implying a forward EBITDA multiple of 6.0 times. The fair value of the put/call option liability of $29,828,000 has been determined based on the forecast financial performance of Outware for the 12 months ending 30 June 2017 and on the expected EBITDA multiple that will be paid.

The dividend liability represents the estimated amount to be paid out to non-controlling interests for the financial periods ending 30 June 2016 and 30 June 2017 as stipulated in the Shareholders Agreement entered between Melbourne IT and non-controlling interests' shareholders. The dividend liability was remeasured at 31 December 2016 based on expected surplus funds derived from the forecast EBITDA consistent with that used in determining the put liability.

Analysis of cash flow on acquisition of Outware, net of cash acquired as at 31 December 2016:

	$'000s
Cash paid on 16 June 2015	22,722
Net cash acquired with Outware	(1,421)
Cash paid for 24.9% of share capital in Outware on 31 August 2016	10,622
	31,923

Transaction costs on acquisition of Uber and Outware

Transaction costs of $1,995,000 have been expensed and are included in other operating expenses. As at 31 December 2015, $1,974,000 has been paid and this is included in the cash flows from investing activities.

Business combinations are accounted for using the acquisition method. The consideration transferred in a business combination is measured at fair value, which shall be calculated as the sum of the acquisition date fair values of the assets transferred by the acquirer, the liabilities incurred by the acquirer to former owners of the acquiree and the equity issued by the acquirer, and the amount of any non-controlling interest in the acquiree. For each business combination, the acquirer measures the non-controlling interest in the acquiree either at fair value or at the proportionate share of the acquiree's identifiable net assets. Acquisition-related costs are expensed as incurred, and included in other expenses.

When the Group acquires a business, it assesses the financial assets and liabilities assumed for appropriate classification and designation in accordance with the contractual terms, economic conditions, the Group's operating or accounting policies and other pertinent conditions as at the acquisition date. This includes the separation of embedded derivatives in host contracts by the acquiree.

If the business combination is achieved in stages, the previously held equity interest is remeasured to the acquisition date fair value and any resulting gain or loss is recognised in profit or loss.

Notes to the Financial Statements

Any contingent consideration to be transferred by the acquirer will be recognised at fair value at the acquisition date. Subsequent changes to the fair value of the contingent consideration which is deemed to be an asset or liability will be recognised in accordance with *AASB 139: Financial Instruments – Recognition and Measurement* either in profit or loss or as a change to other comprehensive income. If the contingent consideration is classified as equity, it is not remeasured until it is finally settled within equity.

D2. Controlled entities

Investments in controlled entities are initially recognised at cost, being the fair value of the consideration given. Following initial recognition, investments are measured at cost less any accumulated impairment losses.

The consolidated financial statements include the financial statements of Melbourne IT Ltd and the subsidiaries in the following table:

Name		Country of Incorporation	Equity Interest %		Cost of Investment $'000	
			2016	2015	2016	2015
WebCentral Group Pty Ltd	(a)	Australia	100	100	78,190	78,190
Netregistry Group Limited	(a) (c)	Australia	100	100	50,436	50,436
Uber Global Pty Ltd	(a)	Australia	100	100	14,909	14,909
Outware Systems Pty Ltd	(a)	Australia	75.1	50.2	33,344	22,722
InfoReady Pty Ltd	(a)	Australia	100	100	15,332	-
Domainz Ltd	(a)	New Zealand	100	100	1,671	1,671
Internet Names Worldwide (US), Inc	(a)	USA	100	100	1	1
Melbourne IT GP Holdings Pty Ltd	(a)	Australia	100	100	-	-
Melbourne IT General Partnership	(b)	USA	100	100	758	758
Advantate Pty Ltd		Australia	100	100	-	-
					194,641	168,687

(a) Investments in controlled entities are initial capital investments and are eliminated in the consolidated financial statements.

(b) Investments in foreign entities are revalued to the year-end foreign exchange spot rates.

(c) Netregistry Group Limited has a 50% ownership in NetAlliance Pty Ltd.

On 30 April 2015, Melbourne IT acquired 100% of Uber Global Pty Ltd and its controlled entities. Refer to note D1 for further details.

On 16 June 2015, Melbourne IT acquired 50.2% of Outware Systems Pty Ltd. On 31 August 2016, the Group exercised its option to purchase further 24.9% of share capital in Outware. Refer to note D1 for further details.

On 31 March 2016, Melbourne IT acquired 100% of InfoReady Pty Ltd. Refer to note D1 for further details.

Notes to the Financial Statements

Summarised statement of profit or loss for Outware

	2016 $’000	2015 $’000
Revenue	24,327	9,987
Cost of sales	(11,173)	(4,215)
Operating expenses	(5,761)	(3,512)
Profit before tax	**7,393**	**2,260**
Income tax	(1,796)	(460)
Profit for the year	**5,597**	**1,800**
Total comprehensive income	**5,597**	**1,800**
Attributable to non-controlling interests	1,839	896
Dividends paid to non-controlling interests	1,329	224

Summarised statement of financial position for Outware

	2016 $’000	2015 $’000
Current assets	7,987	6,810
Non-current assets	885	1,060
Current liabilities	(2,954)	(2,509)
Non-current liabilities	(188)	(890)
Total equity	**5,730**	**4,471**
Attributable to:		
Equity holders of the parent	4,303	2,244
Non-controlling interests	1,427	2,227
Summarised cash flow information for Outware		
Operating	6,142	188
Investing	(307)	(100)
Financing	(4,338)	(450)

Key judgement and estimates

Management’s judgement in assessing that Melbourne IT has control of Outware is based on the consideration of (1) the size of the Melbourne IT’s holding of voting rights relative to the size and dispersion of holdings of the three independent shareholders; (2) Melbourne IT’s potential voting rights via the put options to acquire the remaining 24.9% in 2017; and (3) the power and rights that Melbourne IT has obtained as a result of the strategy outlined in the Business Plan agreed by all shareholders, and its ability to affect the returns and exposures from Outware, are much greater than simply having significant influence.

Notes to the Financial Statements

Section E: Other information

E1. Cash Flow Statement information

	2016 $'000	2015 $'000
Reconciliation of the operating profit after tax to the net cash flow from operations:		
Profit for the year	12,708	6,728
Depreciation of non-current assets	3,537	3,163
Amortisation of non-current assets	3,518	2,413
Expense of share based payments	622	514
Transaction costs	595	1,995
Unwinding of discount on other financial liabilities	504	467
Gain on sale of IDNR business, net of transaction costs	(2,350)	-
Other income	(1,610)	-
Fair value movement in embedded derivatives	59	-
Loss on conversion of Tiger Pistol convertible notes	325	-
Loss on conversion of Tiger Pistol convertible notes	(546)	-
Imputed interest income on convertible note receivables	(133)	-
Changes in assets and liabilities		
(Increase)/ decrease in trade debtors	(3,746)	442
Decrease in prepayments	16	887
Decrease/ (increase) in current tax receivables/ liabilities	1,767	(186)
(Increase) in provisions	(121)	(881)
Decrease in deferred tax asset	1,031	774
(Decrease)/ increase in deferred tax liability	(49)	785
Increase/ (decrease) in accounts payable	580	(1,225)
Decrease in income received in advance	(2,457)	(1,050)
Increase/ (decrease) in other assets	52	(1,203)
Net cash flow from operating activities	**14,302**	**13,623**

Notes to the Financial Statements

Reconciliation of cash and cash equivalents

Cash and short-term deposits in the statement of financial position comprise cash at bank and on hand and short-term deposits with an original maturity of three months or less.

For the purposes of the Statement of Cash Flows, cash and cash equivalents comprise the following:

Cash and cash equivalents on hand	16,426	12,370
Closing cash and cash equivalents balances	**16,426**	**12,370**

E2. Related party disclosures

Ultimate parent

The ultimate Australian Parent entity in the wholly owned Group is Melbourne IT Ltd. During the year various intercompany transactions were undertaken between companies in the wholly owned Group. These transactions were undertaken on a net margin basis. The effect of these transactions are fully eliminated on consolidation. All intercompany balances, payable and receivable, are on an "arm's length" basis with standard terms and conditions.

Other related party transactions

There were no other transactions with related parties during the year ended 31 December 2016 or 2015 other than detailed within the annual report.

E3. Key Management Personnel (KMP) disclosures

For the purposes of this report, the KMP in 2016 are the Martin Mercer - Chief Executive Officer/Managing Director, Peter Findlay - Chief Financial Officer, Brett Fenton - Chief Technology Officer, Amy Rixon - Chief People Officer, Peter Wright - Managing Director, Enterprise Services (ES) and Emma Hunt - Managing Director, SMB.

(a) Remuneration of Key Management Personnel

	2016 $'000	2015 $'000
Compensation of Key Management Personnel		
Short term benefits	2,802	3,838
Post Employment	191	274
Long term benefits	33	29
Termination payments		-
Share-based Payment	528	515
	3,554	4,656

(b) Other transactions and balances with Key Management Personnel

Sales to Key Management personnel are made at arm's length at normal market prices and on normal commercial terms and are negligible.

Notes to the Financial Statements

E4. Performance rights

The Melbourne IT Long Term Incentive Plans ('LTI Plan') have been established where the managing director and employees of the Company are issued with performance rights (zero price options), over the ordinary shares in Melbourne IT Ltd. The performance rights, issued for nil consideration, are issued in accordance with performance guidelines established by the directors of Melbourne IT Ltd. The performance rights cannot be transferred and will not be quoted on the ASX. The managing director and some employees of the company or any of its related body corporate are eligible to participate in the LTI Plan.

Each option is to subscribe for one fully paid Share. When issued, the Share will rank equally with other Shares. The performance rights are not transferable except to the legal personal representative of a deceased or legally incapacitated option holder.

Performance Rights Plan issued from 1 January 2014, have two performance conditions. 50% of the Performance Rights will vest based on the increase in underlying earnings per share ('EPS'), and 50% will vest based on relative total shareholder return ('TSR') in comparison to a peer group from the S&P/ ASX Small Ordinaries Index.

The Performance Rights vest on a sliding scale so that the amount of Rights vesting to the individual depends on the performance level achieved. Performance will be measured over the 36 month period from 1 January of the respective grant year to 31 December of the respective vesting year and will be settled in the equivalent number of ordinary shares of Melbourne IT.

The fair value was determined by an external valuer using a Monte Carlo Simulation Model. In valuing equity-settled transactions, no account was taken of any performance conditions, other than conditions linked to the price of the shares of Melbourne IT Ltd ('market conditions').

The cost of equity-settled transactions will be recognised, together with a corresponding increase in equity, over the period in which the performance conditions are fulfilled, ending on the date on which the relevant employees became fully entitled to the award ('vesting date').

The cumulative expense recognised for equity-settled transactions at each reporting date until vesting date reflected (i) the extent to which the vesting period had expired and (ii) the number of awards that, in the opinion of the directors of Melbourne IT Ltd, would ultimately vest. This opinion was formed based on the best available information at the reporting date.

No expense was recognised for awards that do not ultimately vest, except for awards where vesting was conditional upon a market condition. Where the terms of an equity-settled award were modified, as a minimum an expense was recognised as if the terms had not been modified. In addition, an expense was recognised for any increase in the value of the transaction as a result of the modification, as measured at the date of modification.

The dilutive effect, if any, of outstanding Performance Rights was reflected as additional share dilution in the computation of earnings per share.

The Board has adopted certain policies concerning the terms of the performance rights to be granted under the LTI Plan. The Board has the absolute discretion to change these policies at any time, although any change in its policies will have an effect only on performance rights that are issued at or after the time of the change.

Notes to the Financial Statements

Performance Rights relating to the 31 December 2016 financial year (hereafter referred to as 2016 LTI Plan) were issued on 27 May 2016 in respect to the performance rights granted to the Chief Executive Officer (CEO) and other eligible employees. The 2016 LTI Plan and the performance rights granted to the CEO were approved by shareholders in the Annual General Meeting on 27 May 2016.

Performance Rights relating to the 31 December 2015 financial year (hereafter referred to as 2015 LTI Plan) were issued on 27 May 2015 in respect to the performance rights granted to the Chief Executive Officer (CEO), while the performance rights granted to other eligible employees were issued on 30 March 2015. The 2015 LTI Plan and the performance rights granted to the CEO were approved by shareholders in the Annual General Meeting on 27 May 2015.

The expected life of the performance rights is based on historical data and is not necessarily indicative of exercise patterns that may occur. The expected volatility reflects the assumptions that the historical volatility is indicative of future trends, which may also not necessarily be the actual outcome.

(a) Rights held at the beginning of the reporting period:

There were 1,388,914 Rights held as at the beginning of the reporting period in relation to 2014 and 2015 LTI Plans.

As at 1 January 2016, no performance rights were exercisable.

(b) Rights granted during the reporting period:

The following table summarises the movement in Performance Rights issued during the year:

	2016 Number	2015 Number
Outstanding at the beginning of the year	1,388,914	296,610
Granted during the year	529,178	1,177,383
Vested/exercised during the year	-	-
Lapsed/forfeited during the year	(212,408)	(85,079)
Outstanding at year end	**1,705,684**	**1,388,914**

(c) Rights vested/exercised during the reporting period:

No Rights were vested/exercised during the year ended 31 December 2016 (2015: Nil).

(d) Rights forfeited during the reporting period:

A total of 212,408 (2015: 85,079) Rights were forfeited with a weighted average exercise price of Nil (2015: Nil), by employees during the year.

Notes to the Financial Statements

(e) Rights held at the end of the reporting period:

The following table summarises information about performance rights held by directors and employees as at 31 December 2016:

LTI Plan	Number of Rights	Grant Date	Vesting Date	Expiry Date	Weighted Average Exercise Price
2014 LTI Plan[1]	296,610	27/05/14	31/03/17	31/03/17	$ -
2014 LTI Plan	363,303	12/01/15	31/03/17	31/03/17	$ -
2015 LTI Plan	317,987	30/03/15	31/03/18	31/03/18	$ -
2015 LTI Plan[2]	285,252	27/05/15	31/03/18	31/03/18	$ -
2016 LTI Plan[3]	442,532	27/05/16	31/03/19	31/03/19	$ -
	1,705,684				

1. Rights granted to the CEO for the 2014 plan were approved the 2014 AGM.
2. Rights granted to the CEO for the 2015 plan were approved the 2015 AGM.
3. The 2016 LTI Plan includes rights granted pf 529,178 less rights forfeited of 86,646.

(f) Pricing model: LTI Plans

The fair values of the equity-settled share based payments granted under the 2015 and 2016 LTI Plans are estimated as at the date of grant using a combination of the Monte Carlo simulation methodology (for market based vesting conditions) and discounted cashflow approach (for non-market based vesting conditions).

The following table lists the inputs to the models used for the LTI Plans:

	2016 LTI Plan	2015 LTI Plan
Share price ($)	1.77	1.35 - 1.47
Dividend yield	2.7%	3.5%
Expected volatility	31.0%	31.0% - 32.0%
Risk-free interest rate	1.61%	1.73% -2.02%

The dividend yield is based on historical and future yield estimates. The expected volatility was determined using the group's three year share price.

The risk-free rate is derived from the yield on Australian Government Bonds of an appropriate term.

The weighted average fair value of the performance rights granted during the year was $1.29 (2015: $1.08).

Key judgement and estimates

The fair value is determined by an external valuer using a binomial model and/or Monte Carlo simulation model. In valuing equity-settled transactions, no account is taken of any performance conditions, other than conditions linked to the price of the shares of Melbourne IT Ltd ('market conditions').

Notes to the Financial Statements

E5. Auditors' remuneration

	2016 $	2015 $
Amounts received or due and receivable by the auditors of Melbourne IT Ltd for:		
Audit or review of the financial statements of the entity and any other entity in the consolidated entity	328,570	328,700
Other services in relation to the entity and any other entity in the consolidated entity:		
- Taxation advice	55,275	92,250
- Tax compliance	-	70,500
- Assurance and advisory related	113,676	86,000
	497,521	**577,450**
Amounts received or due and receivable by non Ernst & Young audit firms for:		
Tax compliance services	38,545	94,132
Other non-audit services	219,500	154,000
	258,045	**248,132**

E6. Contingent assets and liabilities

The Group is not aware of the existence of any contingent assets at balance date.

The Group is subject to claims from time to time in the ordinary course of business. There are currently no claims against the Group of individual significance.

E7. Events subsequent to balance date

On 22 February 2017, the directors declared a final dividend of 6.0 cents per ordinary share, franked at 100%, amounting to $6,052,000. The expected payment date of the dividend is 28 April 2017.

On 16 February 2017, the Group entered into a Deed of Variation and Option Exercise with the owners of the non-controlling interest of Outware to purchase the remaining 24.9% of share capital for a total consideration of $28,692,000. Of the consideration paid, $1,000,000 will be held in escrow in the form of shares in Melbourne IT Group, and $2,683,000 will be held in escrow in cash until 31 December 2017, contingent on the employment of the vendors of the non-controlling interest by the Group until that date. This will extinguish the Group's put option and dividend liability to non-controlling interests in Outware. No further payment is due to the vendors of Outware. The total consideration paid for Outware (net of cash acquired) $60,615,000, implying a forward EBITDA multiple of 4.9 times.

Notes to the Financial Statements

The acquisition of the remaining non-controlling interest has been brought forward in order to accelerate the integration of the Outware operations into the Group.

There has not been any other matter or circumstance, in the interval between the end of the financial year and the date of this report that has materially affected, or may materially affect the operations of the consolidated entity, the results of those operations, or the state of affairs of the consolidated entity in subsequent financial periods.

E8. Information relating to Melbourne IT Ltd (the Parent Entity)

	2016 $'000	2015 $'000
Current assets	9,791	13,798
Total assets	214,031	195,259
Current liabilities	63,576	69,223
Total liabilities	114,906	108,428
Contributed equity	51,026	35,629
Options reserve	1,398	776
Hedging reserve	3	(82)
AFS reserve	-	498
Retained earnings	46,698	50,010
	99,125	**86,831**
Profit/ (Loss) of parent entity	2,720	(2,509)
Total comprehensive (loss) of the parent entity	2,307	(2,124)

The parent has issued the following guarantees in relation to the debts of its subsidiaries:

Pursuant to Class Order 98/1418, Melbourne IT Ltd, WebCentral Group Pty Ltd, WebCentral Pty Ltd, Netregistry Group Limited and its controlled entities, Uber Global Pty Ltd and its controlled entities and InfoReady Pty Ltd have entered into a Deed of Cross Guarantee. The effect of the deed is that Melbourne IT Ltd has guaranteed to pay any deficiency in the event of winding up of any controlled entity or if they do not meet their obligations under the terms of overdrafts, loans, leases or other liabilities subject to the guarantee. The controlled entities have also given a similar guarantee in the event that Melbourne IT Ltd is wound up or if it does not meet its obligations under the terms of overdrafts, loans, leases or other liabilities subject to the guarantee.

Notes to the Financial Statements

E9. Closed group class order disclosures

Entities subject to class order relief

Pursuant to Class Order 98/1418, relief has been granted to Melbourne IT Ltd, WebCentral Group Pty Ltd and WebCentral Pty Ltd, Netregistry Group Limited and its controlled entities, Uber Global Pty Ltd and its controlled entities and InfoReady Pty Ltd from the Corporations Act 2001 requirements for the preparation, audit and lodgement of their financial reports.

The consolidated statement of comprehensive income and statement of financial position of the entities that are members of the Closed Group are as follows:

	Closed Group	
	2016	**2015**
	$'000	**$'000**
Consolidated statement of comprehensive income		
Profit before income tax	16,446	7,577
Income tax (expense)/ benefit	(5,538)	(2,708)
Net profit for the period	**10,908**	**4,869**
Retained earnings at the beginning of the period	87,444	82,163
Transfer from options reserve	-	5,059
Dividends provided for or paid	(6,032)	(4,647)
Retained earnings at the end of the period	**92,320**	**87,444**

Notes to the Financial Statements

The consolidated statement of financial position of the entities that are members of the Closed Group are as follows:

	Closed Group	
	2016	**2015**
	$’000	**$’000**
Consolidated statement of financial position		
ASSETS		
Current assets		
Cash and cash equivalents	13,762	11,235
Trade and other receivables	22,682	6,731
Prepayments of domain name registry charges	6,509	9,086
Current tax receivable	-	424
Derivative financial instruments	4	-
Other assets	3,340	2,874
Total current assets	**46,297**	**30,350**
Non-current assets		
Property, plant and equipment	6,386	7,196
Intangible assets	152,587	134,652
Deferred tax assets	3,932	4,955
Prepayments of domain name registry charges	2,964	4,987
Non-current financial assets	1,795	1,995
Other assets	32,433	32,519
Total non-current assets	**200,097**	**186,304**
TOTAL ASSETS	**246,394**	**216,654**

Notes to the Financial Statements

LIABILITIES		
Current liabilities		
Trade and other payables	16,340	16,778
Interest bearing loans and borrowings	92	198
Current tax payable	1,560	-
Provisions	2,936	3,016
Derivative financial instruments	-	117
Income received in advance	23,788	27,550
Total current liabilities	**44,716**	**47,659**
Non-current liabilities		
Interest bearing loans and borrowings	36,536	30,144
Deferred tax liability	2,329	1,935
Provisions	688	495
Income received in advance	8,912	11,846
Other financial liabilities	8,315	-
Total non-current liabilities	**56,780**	**44,420**
TOTAL LIABILITIES	101,496	92,079
NET ASSETS	144,898	124,575
EQUITY		
Contributed equity	51,026	35,629
Options reserve	1,398	776
Hedging reserve	3	(82)
Non-controlling interest	151	310
AFS reserve	-	498
Retained earnings	92,320	87,444
TOTAL EQUITY	144,898	124,575

E10. New accounting policies

The accounting policies adopted are consistent with those of the previous financial year except as follows:

The Group has adopted the following new and amended Australian Accounting Standards as of 1 January 2016.

AASB 2014-4 Clarification of Acceptable Methods of Depreciation and Amortisation (Amendments to AASB 116 and AASB 138)

AASB 116 *Property Plant and Equipment* and AASB 138 *Intangible Assets* both establish the principle for the basis of depreciation and amortisation as being the expected pattern of consumption of the future economic benefits of an asset. The IASB has clarified that the use of revenue-based methods to calculate the depreciation of an asset is not appropriate

Notes to the Financial Statements

because revenue generated by an activity that includes the use of an asset generally reflects factors other than the consumption of the economic benefits embodied in the asset. The amendment also clarified that revenue is generally presumed to be an inappropriate basis for measuring the consumption of the economic benefits embodied in an intangible asset. This presumption, however, can be rebutted in certain limited circumstances.

AASB 2015-2 Amendments to Australian Accounting Standards - Disclosure Initiative: Amendments to AASB 101

The Standard makes amendments to AASB 101 *Presentation of Financial statements* arising from the IASB's Disclosure Initiative project. The amendments are designed to further encourage companies to apply professional judgement in determining what information to disclose in the financial statements. For example, the amendments make clear that materiality applies to the whole financial statements and that the inclusion of immaterial information can inhibit the usefulness of financial disclosures. The amendments also clarify that companies should use professional judgement in determining where and in what order information is presented in the financial disclosures.

AASB 2015-3 Amendments to Australian Accounting Standards arising from the Withdrawal of AASB 1031 Materiality

The Standard completes the AASB's project to remove Australian guidance on materiality from Australian Accounting Standards.

AASB 2015-9 Amendments to Australian Accounting Standards - Scope and Application Paragraphs (AASB 8, AASB 133 & AASB 1057)

This Standard insert scope paragraphs into AASB 8 *Operating Segments* and AASB 133 *Earnings per Share* in place of application paragraph test in AASB 1057 *Application of Australian Accounting Standards*. This is to correct inadvertent removal of these paragraphs during editorial changes made in August 2015. There is no change to the requirements or the applicability of AASB 8 and AASB 133.

The adoption of the above standards/improvements had no material impact on the financial position or performance of the Group.

The Group has not early adopted any other standard, interpretation or amendment that has been issued but is not yet effective.

(ii) Accounting Standards and Interpretations issued but not yet effective

Australian Accounting Standards that have recently been issued or amended but which are not yet effective and have not been adopted by the Group for the annual reporting period ended 31 December 2016 are outlined in the table below.

Reference	Title	Summary	Application Date of Standard*	Impact on Group Financial Report	Application Date for Group*
2016-1	Amendments to Australian Accounting Standards - Recognition of Deferred Tax Assets for Unrealised Losses (AASB 112)	This Standard amends AASB 112 *Income Taxes* (July 2004) and AASB 112 *Income Taxes* (August 2015) to clarify the requirements on recognition of deferred tax assets for unrealised losses on debt instruments measured at fair value.	1-Jan-17	Whilst the impact of the application of the new Standard is currently being assessed, our initial assessment is that there should be no material impact on the Group's	1-Jan-17

Notes to the Financial Statements

Reference	Title	Summary	Application Date of Standard*	Impact on Group Financial Report	Application Date for Group*
				financial position or performance.	
2016-2	Amendments to Australian Accounting Standards - Disclosure Initiative: Amendments to AASB 107	This Standard amends AASB 072 *Statement of Cash Flows* (August 2015) to require entities preparing financial statements in accordance with Tier 1 reporting requirements to provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes from cash flows and non-cash changes.	1-Jan-17	There should be no material impact on the Group's financial position or performance.	1-Jan-17
AASB 16	Leases	The key features of AASB 16 are as follows: Lessee accounting • Lessees are required to recognise assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value. • A lessee measures right-of-use assets similarly to other non-financial assets and lease liabilities similarly to other financial liabilities. • Assets and liabilities arising from a lease are initially measured on a present value basis. The measurement includes non-cancellable lease payments (including inflation-linked payments), and also includes payments to be made in optional periods if the lessee is reasonably certain to exercise an option to extend the lease, or not to exercise an option to terminate the lease. • AASB 16 contains disclosure requirements for lessees Lessor accounting	1-Jan-19	The impact of the application of the new Standard is currently being assessed.	1-Jan-19

Notes to the Financial Statements

Reference	Title	Summary	Application Date of Standard*	Impact on Group Financial Report	Application Date for Group*
		• AASB 16 substantially carries forward the lessor accounting requirements in IAS 17. Accordingly, a lessor continues to classify its leases as operating leases or finance leases, and to account for those two types of leases differently • AASB 16 also requires enhanced disclosures to be provided by lessors that will improve information disclosed about a lessor's risk exposure, particularly to residual value risk.			
AASB 9	Financial instruments	AASB 9 (December 2014) is a new standard which replaces AASB 139. This new version supersedes AASB issued in December 2009 and December 2010. It includes a model for classification and measurement, a single forward-looking 'expected loss' impairment model and a substantially-reformed approach to hedge accounting. New hedge accounting requirements including changes to hedge effectiveness testing, treatment of hedging costs, risk components that can be hedged and disclosures. AASB 9 is effective for annual periods beginning on or after 1 January 2018. However, the Standard is available for early adoption. The own credit changes can be early adopted in isolation without otherwise changing the accounting for financial instruments. Consequential amendments were also made to other standards as a result of AASB 9, introduced by AASB 2009-11 and superseded by AASB 2010-7, 2010-10 and 2014-1- Part E. AASB 2014-7 incorporates the consequential amendments arising from the issuance of AASB	1-Jan-18	Whilst the impact of the application of the new Standard is currently being assessed, our initial assessment is that there should be no material impact on the Group's financial position or performance.	1-Jan-18

Notes to the Financial Statements

Reference	Title	Summary	Application Date of Standard*	Impact on Group Financial Report	Application Date for Group*
		9 in December 2014. AASB 2014-8 limits the application of the existing versions of AASB 9 (AASB 9 December 2009 and AASB 9 December 2010) from 1 February 2015 and applies to annual reporting periods beginning on or after 1 January 2015.			
IFRS 2 (Amend-ments)	Classification and Measurement of Share-based Payment Transactions (Amendments to IFRS 2)	This standard amends to IFRS 2 share-based Payment, clarifying how to account for certain types of share-based payment transactions. The amendments provide requirements on the accounting for: - The effects of vesting and non-vesting conditions on the measurement of cash-settled share-based payments - Share-based payment transactions with a net settlement feature for withholding tax obligations - A modification to the terms and conditions of a share-based payment that changes the classification of the transaction from cash-settled to equity-settled.	1-Jan-18	Whilst the impact of the application of the new Standard is currently being assessed, our initial assessment is that there should be no material impact on the Group's financial position or performance.	1-Jan-18
AASB 15	Revenue from Contracts with Customers	AASB 15 Revenue from Contracts with Customers replaces the existing revenue recognition standards AASB 111 *Construction Contracts*, AASB 118 *Revenue* and related Interpretations (Interpretation 13 *Customer*	1-Jan-18	The impact of the application of the new Standard is currently being assessed.	1-Jan-18

Notes to the Financial Statements

Reference	Title	Summary	Application Date of Standard*	Impact on Group Financial Report	Application Date for Group*
		Loyalty Programmes, Interpretation 15 *Agreements for the Construction of Real Estate*, Interpretation 18 *Transfers of Assets from Customers*, Interpretation 131 *Revenue—Barter Transactions Involving Advertising Services* and Interpretation 1042 *Subscriber Acquisition Costs in the Telecommunications Industry*). AASB 15 incorporates the requirements of AASB 15 Revenue from Contracts with Customers issued by the International Accounting Standards Board (IASB) and developed jointly with the US Financial Accounting Standards Board (FASB). AASB 15 specifies the accounting treatment for revenue arising from contracts with customers (except for contracts within the scope of other accounting standards such as leases or financial instruments). The core principle of AASB 15 is that an entity recognises revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. AASB 2015-8 amended the AASB 15 effective date so it is now effective for annual reporting periods commencing on or after 1 January 2018. Early application is permitted. AASB 2014-5 incorporates the consequential amendments to a number of Australian Accounting Standards (including Interpretations) arising from the issuance of AASB 15. AASB 2016-3 Amendments to Australian Accounting Standards - Clarifications to AASB 15 amends AASB 15 to clarify the requirements on identifying performance obligations, principal			

Notes to the Financial Statements

Reference	Title	Summary	Application Date of Standard*	Impact on Group Financial Report	Application Date for Group*
		versus agent considerations and the timing of recognising revenue from granting a licence and provides further practical expedients on transition to AASB 15.			

* Application date is for the reporting periods beginning on or after the date shown in the above table

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Independent Auditor's Report

To the Shareholders of Melbourne IT Limited

Report on the Audit of the Financial Report

Opinion

We have audited the financial report of Melbourne IT Limited (the Company) and its subsidiaries (the Group), which comprises the consolidated statement of financial position as at 31 December 2016, the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, notes to the financial statements, including a summary of significant accounting policies, and the directors' declaration.

In our opinion, the accompanying financial report of the Group is in accordance with the *Corporations Act 2001*, including:

a. giving a true and fair view of the consolidated financial position of the Group as at 31 December 2016 and of its consolidated financial performance for the year ended on that date; and

b. complying with Australian Accounting Standards and the *Corporations Regulations 2001*.

Basis for Opinion

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Group in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

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

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial report of the current year. These matters were addressed in the context of our audit of the financial report as a whole, and in forming our opinion thereon, but we do not provide a separate opinion on these matters. For each matter below, our description of how our audit addressed the matter is provided in that context.

We have fulfilled the responsibilities described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the financial report. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying financial report.

Recoverable value of goodwill and other intangibles assets

Why significant	How our audit addressed the key audit matter
At 31 December 2016 the Group's goodwill and other intangible assets balance is $222.0 million which represents 78% of total assets. The Directors assessment of the recoverable value of the goodwill and other intangible assets has been identified as a key audit matter and significant to the audit as the assessment process is complex and judgemental and is based on assumptions relating to future market or economic conditions. In performing the recoverability assessment, the Group has applied various assumptions with respect to revenue and cashflow growth rates based on expectations and estimates of future results of the cash generating units. The Group has disclosed in note B3 to the financial statements the assessment method, including the main underlying assumptions, the results of the assessment as well as the impact of applying sensitivities.	Our audit procedures assessed and tested the assumptions and methodologies used in the Group's goodwill and other intangible assets impairment model, which underpins the Directors assessment. This included assessing the support for the forecast cash flows, working capital levels, allocation of corporate costs and the discount rate used. We assessed the level at which goodwill is monitored and evaluated the identification of cash generating units. Furthermore, we assessed the historical accuracy of the Group's forecasts, compared the market capitalisation of the company to the Group's net assets and analysed sensitivities. We involved our valuation specialists to assist with comparing the Group's discount rates and long term growth rate assumptions to external data and benchmarking the implied earnings multiples to comparable companies. We assessed the adequacy of the Group's disclosures in Note B3 concerning the key assumptions and sensitivities.

Acquisition accounting

Why significant	How our audit addressed the key audit matter
On 31 March 2016, Melbourne IT Limited acquired 100% of the shares of InfoReady Pty Ltd (InfoReady) for purchase consideration of$15.3 million and contingent consideration. Note D1 to the financial statements discloses details of the contingent consideration. . The accounting for the acquisition of InfoReady has been identified as a key audit matter as the acquisition is material, the accounting required significant judgement, including the purchase price allocation and the identification and determination of the fair value of assets and liabilities acquired as well as the contingent consideration Melbourne IT Limited engaged external valuation experts to determine the fair value of the identifiable intangible assets acquired. As part of the acquisition of Outware Systems Pty Ltd (Outware) on 16 June 2015, Melbourne IT acquired 50.2% of the shares in Outware for$22.7 million with put and call options to acquire the remaining shares in Outware over 2 years. At 31 December 2016, Melbourne IT Limited had a put option to acquire the remaining 24.9% Accounting for the subsequent reassessment of the put option required significant judgement in relation to the estimates involved with assessing the fair value of the put option. Note D1 to the financial statements discloses the final fair values of assets and liabilities acquired and contingent liabilities assumed, together with a reconciliation to the provisional accounting which was included in the 30 June 2016 half year financial report. Note C6 discloses the fair value of the put option liability.	Our audit procedures considered the purchase agreement, consideration paid and the allocation of the purchase consideration to the fair value of assets and liabilities acquired. We assessed the identification and valuation of the assets and liabilities acquired, and the contingent consideration recognised. This included reassessing the Directors' estimates with respect to the fair value of the contingent consideration at year end. We assessed the competence, independence and relevant experience of the external valuation expert engaged by Melbourne IT Limited to value the identifiable intangible assets. We involved our valuation specialists to assess the methodologies and assumptions used to determine fair values. We also involved our tax specialists to assess the recognition and valuation of resulting deferred tax assets and liabilities. In respect of the acquisition of Outware, we assessed the Directors' estimates with respect to the fair value of the put option liability. We considered the adequacy of the related disclosures made in the notes to the financial statements.

Building a better working world

Revenue recognition

Why significant	How our audit addressed the key audit matter
The Group offers many products and services to its customers that require different revenue recognition accounting policies given different performance obligation profiles, as outlined in note A1 to the financial statements. In particular, revenue for domain names and fixed priced contracts is recognised by reference to the percentage of completion method. Revenue recognition has been assessed as a key audit matter due to the different recognition policies, the judgment involved in determining the percentage of completion and the risk that revenue may be recognised prematurely as often all of the revenue to be earned under a customer contract is received upon entering into the contract.	Our audit procedures included considering the appropriateness of the Group's revenue recognition accounting policies, in particular those products and services where revenue is recognised based on the percentage of completion. We assessed the design and operating effectiveness of the Group's controls, including automated controls, over the initial recognition of transactions, the deferred revenue and related cost of sales calculations. We agreed details back to contracts for individually significant contracts and assessed the assumptions used by the Group in the determination of the percentage of completion. We assessed sales transactions taking place before and after year end to check whether the revenue was recognised in the correct period.

Information Other than the Financial Statements and Auditor's Report

The directors are responsible for the other information. The other information comprises the information included in the Group's 2016 Annual Report other than the financial report and our auditor's report thereon. We obtained the Directors' Report that is to be included in the Annual Report, prior to the date of this auditor's report, and we expect to obtain the remaining sections of the Annual Report after the date of this auditor's report.

Our opinion on the financial report does not cover the other information and we do not and will not express any form of assurance conclusion thereon.

In connection with our audit of the financial report, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial report or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If, based on the work we have performed on the other information obtained prior to the date of this auditor's report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the Directors for the Financial Report

The directors of the Company are responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal control as the directors determine is necessary to enable the preparation of the financial report that gives a true and fair view and is free from material misstatement, whether due to fraud or error.

In preparing the financial report, the directors are responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Group or to cease operations, or have no realistic alternative but to do so.

Auditor's Responsibilities for the Audit of the Financial Report

Our objectives are to obtain reasonable assurance about whether the financial report as a whole is free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the Australian Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of this financial report.

A further description of our responsibilities for the audit of the financial report is located at the Auditing and Assurance Standards Board website at: http://www.auasb.gov.au/Home.aspx. This description forms part of our auditor's report.

Report on the Audit of the Remuneration Report

Opinion on the Remuneration Report

We have audited the Remuneration Report included in pages 36 to 48 of the Directors' Report for the year ended 31 December 2016.

In our opinion, the Remuneration Report of Melbourne IT Limited for the year ended 31 December 2016, complies with section 300A of the *Corporations Act 2001*.

Responsibilities

The directors of the Company are responsible for the preparation and presentation of the Remuneration Report in accordance with section 300A of the *Corporations Act 2001*. Our responsibility is to express an opinion on the Remuneration Report, based on our audit conducted in accordance with Australian Auditing Standards.

Ernst & Young

Ernst & Young

David Petersen
Engagement Partner
Melbourne
30 March 2017

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Auditor's Independence Declaration to the Directors of Melbourne IT Limited

As lead auditor for the audit of Melbourne IT Limited for the financial year ended 31 December 2016, I declare to the best of my knowledge and belief, there have been:

a) no contraventions of the auditor independence requirements of the *Corporations Act 2001* in relation to the audit; and

b) no contraventions of any applicable code of professional conduct in relation to the audit.

This declaration is in respect of Melbourne IT Limited and the entities it controlled during the financial year.

Ernst & Young

Ernst & Young

David Petersen
Partner
30 March 2017

ASX Additional Information

Additional information required by the Australian Stock Exchange Ltd Listing Rules and not shown elsewhere in this report is as follows. The following information was current as at 21 March 2017.

Distribution schedule of the equity security holders

The distribution schedule of the number of holders in each class of equity securities are as follows:

Range	Ordinary Share Holders	Performance Rights Holders
100,001 and Over	45	7
50,001 to 100,000	47	-
10,001 to 50,000	675	-
5,001 to 10,000	785	-
1,001 to 5,000	2,314	-
1 to 1,000	1,535	-
Total number of equity security holders	5,401	7

As at the close of trading on 21 March 2017, the Company's share price was $2.15 Based on this closing price, there were 298 shareholders holding less than a marketable parcel of 233 ordinary shares.

The 20 largest security holders

The names of the 20 largest holders of quoted equity securities, and the number of equity securities and percentage of capital each holds, are listed below.

	Name of Registered Security Holder	Number of Ordinary Shares held	Percentage of Issued Ordinary Shares
1	HSBC Custody Nominees (Australia) Limited	20,887,051	20.71
2	J P Morgan Nominees Australia Limited	10,899,032	10.81
3	Corpsand Pty Ltd <The Impulse A/C>	9,208,363	9.13
4	BNP Paribas Nominees Pty Ltd <Agency Lending DRP A/C>	5,317,148	5.27
5	Sieana Pty Ltd <KKT A/C>	2,848,399	2.82
6	Citicorp Nominees Pty Limited	2,785,033	2.76
7	RBC Investor Services Australia Nominees Pty Limited <BKCUST A/C>	2,539,730	2.52
8	York Investments Limited	2,533,823	2.51
9	National Nominees Limited	2,449,697	2.43
10	Citicorp Nominees Pty Limited <Colonial First State Inv A/C>	2,010,577	1.99
11	BNP Paribas Noms Pty Ltd <DRP>	1,601,067	1.59
12	KTAP Pty Ltd	783,490	0.78
13	Mount Ida Holdings Pty Ltd <Stewart Super Fund A/C>	773,539	0.77
14	National Nominees Limited <DB A/C>	701,322	0.70
15	McNeil Nominees Pty Limited	500,000	0.50

ASX Additional Information

	Name of Registered Security Holder	Number of Ordinary Shares held	Percentage of Issued Ordinary Shares
16	Querion Pty Ltd	314,427	0.31
17	Forsyth Barr Custodians Ltd <Forsyth Barr Ltd-Nominee A/C>	275,569	0.27
18	Principal Funds Management Co Pty Ltd <Principal Growth A/C>	250,000	0.25
18	Pubdin Pty Ltd	250,000	0.25
19	Mr David Goldberg & Ms Bella Goldberg & Mr Michael Goldberg <Goldberg Family S/F A/C>	245,000	0.24
20	Sieana Pty Ltd	234,941	0.23
	Sub-Total	67,408,208	66.83
	Balance of register	33,453,122	33.17
	Total	100,861,330	100.00

Unquoted equity securities

As at 21 March 2017, there were 1,705,684 unlisted performance rights over unissued ordinary shares in the Company, granted to 7 holders.

Voting rights

The voting rights attaching to each class of equity securities are as follows:

(a) Ordinary Shares - All ordinary shares carry one vote per share without restriction.

(b) Performance Rights - Performance Rights do not carry any voting rights.

Substantial holders

The names of substantial holders in the Company and the number of securities to which each substantial holder and their associates have a relevant interest are listed below. The following information is extracted from the substantial holder notices received by the Company as at 21 March 2017.

Name	Number of Ordinary Shares held	Percentage of Issued Ordinary Shares
Cadence Asset Management Entities	17,280,756	17.13%
Corpsand Pty Ltd atf Impulse Trust	9,208,363	9.91%
IOOF Holdings Limited	7,733,488	7.667%
Sieana Pty Ltd & associated entities	5,721,488	5.70%
BlackRock Group	5,715,787	5.66%

On-market buyback

As at the date of this report, there is no on-market share buyback.

NOTES

Outware
mobile

INFOREADY

MELBOURNE IT

WebCentral

netregistry™

TPP
WHOLESALE

DOMAINZ
THE KIWI WEBXPERTS

Corporate Directory

Melbourne IT Ltd

ABN: 21 073 716 793

Melbourne IT Limited is a publicly listed company, limited by shares. It is incorporated and domiciled in Australia.

Directors

Ms. G. Pemberton (appointed Chair on 1 February 2017)
Mr. S.D. Jones (Chairman to 1 February 2017)
Mr. M. Mercer (Managing Director and CEO)
Mr. J. Armstrong
Mr. L. Bloch
Mr. T. Kiing
Ms. N. Sparks AM
Mr. R.J. Stewart AM (retired 27 May 2016)

Managing Director & Chief Executive Officer

Mr. M. Mercer

Chief Financial Officer

Mr. P. Findlay (Resigned on 20 January 2017)
Mr. S. Bland (Appointed on 27 March 2017)

Company Secretary

Ms. E. Rigato

Stock Exchange Listing

Melbourne IT Limited shares (MLB) are listed on the Australian Stock Exchange.

Registered Office

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Share Registry

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Corporate Governance Statement

www.melbourneit.info/investor-centre/corporate-governance