Annual Report 2017

About Kainos Kainos is a digital services and platforms company, offering information technology products and services to customers in a range of markets, including government, healthcare and financial services. Kainos provides software design and development services and a complementary suite of software products in healthcare and automated testing.

Kainos is now a global business with increasing scale, resilience, ambition and expertise. We've delivered 17% compound growth of revenue in the past three years and we're recognised as a continuing disruptive force in our core markets of government, healthcare and commercial industries.

We're increasingly trusted by our customers, including global organisations such as United Drug Group (UDG) and large UK government departments such as the UK Department for Transport (DfT). We provide them with digital technology solutions that help them conduct their business more efficiently. In healthcare, we are developing genuinely new mobile applications that have the potential to change the way in which clinicians can help patients. In all of our services and products we seek to serve the changing needs of our customers.

Just as we have gained the trust and respect of our customers, we are once again judged by our staff to be one of the best companies to work for. Our people remain our top priority, and we continue to invest in recruiting the best, and providing rewarding and enjoyable careers for them.

Our business model is simple: we recruit the best people and encourage them to deliver exceptional services and products to customers. Everything we do is centred on this core principle, and it has served us well over time.

Kainos is listed on the London Stock Exchange (symbol KNOS).

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Operational highlights

Sixth consecutive year of revenue and adjusted pre-tax profit growth (compound revenue growth of 46% over last six years)

Continued growth in Digital Services driven by existing customer demand:

- Significant ongoing engagements in UK government's digital transformation programme
- Accelerated growth in Workday implementation, and strengthened position as the leading European implementation partner following market consolidation
- Opening of Frankfurt office to support further European expansion

Digital Platforms showing progress against key milestones:

- 37 new Kainos Smart customers, bringing the total on the platform to 92
- Evolve Integrated Care now in live use at 38 hospitals in the US
- Doubled research and development expenditure to £4.6 million (2016: £2.3 million)

Customer approval of Group services rated as 'Good' or better by 92% of customers

Strong recruitment has seen staff increase by 135 to 975 at year end

44th

Fifth consecutive year in the Sunday Times 'Best Companies to Work For' Top 100, ranked 44th

The business is highly cash generative with strong underlying cash conversion

Financial highlights

	2017	2016	Change
Revenue	**£83.5m**	£76.6m	+9%
Adjusted pre-tax profit [1]	**£14.3m**	£14.1m	+1%
Statutory profit before tax	**£13.3m**	£14.3m	-7%
Cash	**£23.7m**	£15.0m	+58%
Sales orders	**£94.8m**	£87.2m	+9%
SaaS sales orders	**£10.1m**	£8.6m	+17%
Backlog [2]	**£76.4m**	£71.5m	+7%
Adjusted diluted earnings per share [1]	**9.5p**	10.5p	-10%
Diluted earnings per share	**8.7p**	10.6p	-18%
Proposed total dividend	**6.3p**	6.0p	+5%

1 Calculated by taking the statutory profit before tax and adding back £0.95 million share-based payments (2016: £0.52 million) and £Nil exceptional items (2016: £0.68 million gain).

2 The value of contracted revenue that has yet to be recognised.

Chief Executive Officer's statement

→ We remain focused on providing exceptional careers for our staff and exceptional digital products and services for our customers.

I am delighted to report another year of growth, in both our domestic and international markets.

For the sixth consecutive year we are reporting strong growth in Digital Services, driven by demand from existing customers, new customer acquisition and geographic expansion. We continue to deliver major transformation programmes across UK government and we have also experienced very strong growth within the Commercial Sector, which is now the fastest growing segment within the division. Client demand across Europe has resulted in the opening of our Frankfurt office, alongside the established offices in Amsterdam and Gdansk.

Our Digital Platforms division continues to make progress, despite the funding challenge in the NHS. The addition of 37 new customers for Smart, our market-leading Software as a Service (SaaS) platform for automated testing of the Workday suite is particularly exciting as it brings the total number of global customers on the platform to 92. Evolve Integrated Care has signed a significant contract with a UK-based NHS Clinical Commissioning Group and post-period end, live operation has started across 38 US hospitals.

We remain focused on providing exceptional careers for our staff and exceptional digital products and services for our customers. The Group's pipeline of prospects continues to strengthen across all divisions and the Board believes that the Group is well-positioned for growth in the coming years.

Dr Brendan Mooney
Chief Executive Officer

Strategic Report

Overview

The financial results for the year ended 31 March 2017 represent the sixth consecutive year of revenue and adjusted pre-tax profit growth, and continued investment, particularly in the Group's Digital Platforms, and provide an excellent platform for future growth.

→ Revenue for the year ended 31 March 2017 grew by 9% to £83.5 million. Adjusted pre-tax profits increased by 1% to £14.3 million.

Revenue for the year ended 31 March 2017 grew by 9% to £83.5 million (2016: £76.6 million). Adjusted pre-tax profits increased by 1% to £14.3 million (2016: £14.1 million), which included expenditure of £4.6 million in research and development (2016: £2.3 million).

Sales orders for this period amounted to £94.8 million (2016: £87.2 million), a total that included £10.1 million (2016: £8.6 million) of SaaS product sales orders, an increase of 17%. The contracted backlog for the Group increased by 7% to £76.4 million (2016: £71.5 million). The proportion of revenue generated from customers outside the UK increased by 40% in 2017 and now accounts for 21% of total Group revenue (2016: 15%).

Staff numbers increased by 135 to 975 at 31 March 2017 (2016: 840). The Group continues to attract very strong interest from both graduates and experienced senior candidates in key employment markets, with 9,380 job applications received during the year; 82% of people joining Kainos were recruited directly rather than via recruitment agencies. Employee engagement remains high, with the Group being ranked in the Sunday Times Top 100 'Best Companies to Work For' for the fifth consecutive year. As a result, attrition across the Group remains very low at 8% (2016: 10%).

Customer satisfaction remains high, with 92% of customers rating Group service 'good' or better. This high level of customer service underpins the Group's long term relationships with customers, with existing customers accounting for 91% of Group revenue. In the year to 31 March 2017, the Group acquired 59 new customers, making a total of 247.

Across sectors, 54% of Group revenue is derived from government customers (2016: 52%), 29% from commercial sector (2016: 23%) and 17% from healthcare (2016: 25%). Commercial sector revenue grew 40% to £24.4 million (2016: £17.4 million).

As previously announced, the Group is now presenting its operations in terms of Digital Services and Digital Platform offerings (rather than by operating division – Digital Services, Evolve, WorkSmart). The directors believe this better represents the Group's business by highlighting more clearly how each offering is positioned in the market, and more easily allowing the application of appropriate performance metrics to each part of the business. Note 25 to the accounts sets out a reconciliation of the previous reporting structure to the new one.

In the year ended 31 March 2017, Digital Services experienced strong growth across both Digital Transformation and Workday Implementation service lines. Workday Implementation services in particular experienced accelerated growth through increased demand from existing customers, new customer acquisition and geographic expansion. The opening of the Frankfurt office is viewed by the Group as an important development in supporting further European expansion.

In the Digital Platforms division, the Kainos Smart automated testing platform continued its growth trajectory, adding 37 new customers during 2017 to bring the total number of customers on the platform to 92 at 31 March 2017.

Evolve EMR continued to face headwinds in 2017 caused by the reduction in funding in the NHS. As a result, Evolve EMR revenue (excluding third party)[1] reduced by 12% to £10.0 million (2016: £11.4 million) which is in line with previous guidance.

Evolve IC achieved a significant milestone after period close, moving to live use across 38 hospitals in a large US Health Network.

As noted above, Group expenditure on research and development increased significantly in the year ended 31 March 2017, with £4.6 million expensed (2016: £2.3 million).

Finally, cash generation was exceptionally high, with a cash balance of £23.7 million at 31 March 2017 (2016: £15.0 million), representing 109% cash conversion[2] (2016: 77%).

1 Third party revenue includes fees charged to customers for third party services and products, such as scanning services and computer hardware. Evolve EMR revenue (including third party) reduced by 27% to £13.8 million (2016: £18.9 million).

2 Calculated as adjusted pre-tax profit adding back finance income and depreciation, divided by cash generated by operations.

Revenue

2017

£83.5m

2016

£76.6m

Finance review

Kainos achieved revenue of £83.5 million, representing a 9% growth on 2016 (£76.6 million). Gross profit margin increased from 48% to 52% mainly because of the decrease in third party revenue[1]. Sales orders for this period amounted to £94.8 million (2016: £87.2 million), a total that included £10.1 million (2016: £8.6 million) of SaaS product sales orders, an increase of 17%.

The proportion of revenue generated outside the UK increased by 40% in 2017 and now accounts for 21% of total Group revenue (2016: 15%). Across sectors, 54% of Group revenue is derived from government customers (2016: 52%), 29% from commercial sector (2016: 23%) and 17% from healthcare (2016: 25%). Commercial sector revenue grew 40% to £24.4 million (2016: £17.4 million).

Operating expenses excluding share-based payments for 2017 increased by 27% to £29.3 million (2016: £23.1 million), largely driven by investment in the Group's Digital Platforms, primarily product development and sales and marketing. As anticipated, investment in product development has continued to grow, with overall expenditure increased by 100% to £4.6 million (2016: £2.3 million), all of which was expensed in the period. Kainos has implemented the Research and Development Expenditure Credit regime ("RDEC") during the period. As a result, research and development credits that were previously offset against the income tax expense are now received in the form of research and development grants and are offset against operating expenses, reducing operating expenses by £1.7 million[3] in the period.

Adjusted pre-tax profit increased by 1% to £14.3 million (2016: £14.1 million). Statutory profit before tax decreased by 7% to £13.3 million (2016: £14.3 million), largely because of the effect of the exceptional gain of £2.0 million in 2016 in relation to the sale of SpeechStorm.

The effective tax rate for 2017 was 22% (2016: 13%). The increase in the effective tax rate is largely due to the impact of research and development credits and the exceptional gain on the SpeechStorm sale in 2016.

The Group has a robust balance sheet with £23.7 million of cash (2016: £15.0 million), no debt and net assets of £30.0 million (2016: £25.9 million). The net cash position increased by £8.7 million due to exceptionally high cash generation during the year ended 31 March 2017. Net cash from operating activities increased by 72% to £16.9 million in the period (2016: £9.8 million) driven by £4.0 million cash generated by working capital, primarily as a result of increased deferred income relating to Smart sales.

Dividend

The final dividend, if approved by shareholders, will be 4.4p and payable on 20 October 2017 to shareholders on the register on 22 September 2017, with an ex-dividend date of 21 September 2017. This will make the total dividend for the year 6.3p (2016: 6.0p).

Business model and strategy

The Kainos vision is to enable outstanding people to create digital solutions that have a positive impact on people's lives. It achieves this by providing innovative Digital Services and Platforms to its customers in public and commercial industry sectors.

Kainos charges for its Digital Services on a time and materials or fixed price basis. In 2017, the majority of service revenue (approximately 88%) was derived from time and materials contracts and the remainder from fixed price contracts. The Group's Digital Platforms are licensed to customers on a recurring annual basis following a SaaS business model and less frequently as a fixed one-off lifetime usage licence (for some Evolve customers). The Group has strong cash generation and a growing level of recurring revenue. This provides increasing stability to the business and allows Kainos to commit to the long term development of its platforms.

→ The proportion of revenue generated outside the UK increased by 40% in 2017 and now accounts for 21% of total Group revenue.

3 The new RDEC Scheme was retrospectively adopted from 2015 and £1.1 million relates to prior periods.

The strategy of the Group is to achieve sustained revenue, adjusted pre-tax profit and cash flow growth in its chosen markets through:

- growing and maintaining the Group's reputation;
- capitalising on its established market position and significant growth opportunities;
- building strong, long term relationships with its customer base;
- exploiting favourable market dynamics and drivers;
- nurturing and expanding its experienced and highly-skilled employee pool; and
- recruiting high calibre entry-level and experienced staff.

Divisional review

Digital Services

The Digital Services division comprises two areas of activity:

- **Digital Transformation:** the delivery of customised online digital solutions, principally for central government, regional government and local government departments and agencies ("UK government") and for commercial sector organisations. The solutions provided are highly cost-effective and make public services more accessible and easier to use for the citizen and customer.
- **Workday Implementation:** the provision of consulting, project management, integration and support services for Workday's Enterprise Resource Planning (ERP) software suite, which includes cloud-based software for Human Capital Management (HCM) and Financial Management that enables enterprises to organise their staff efficiently and to support financial reporting requirements.

Digital Services revenue for the year ended 31 March 2017 grew by 17% to £64.5 million (2016: £55.1 million). Gross profit for the division increased by 23% to £31.2 million (2016: £25.4 million). Digital Services revenue from customers in commercial sectors accounted for £19.7 million (2016: £15.0 million), an increase of 31%. Sales orders in Digital Services increased by 18% to £74.6 million (2016: £63.4 million) and contracted backlog for the division increased by 9% to £36.1 million (2016: £33.0 million).

Adjusted pre-tax profit

2017

£14.3m

2016

£14.1m

Digital Services – Digital Transformation

The UK government's programme of digitisation of public sector services is now well-established. Involved from the early stages of public sector digitisation, Kainos now holds a leading position in the supplier ecosystem, and continues to extend its engagement on flagship transformation programmes for existing and new customers across several departments.

At the Driver and Vehicle Standards Agency, Kainos continues to work on the ambitious IT modernisation programme following its involvement on the highly successful MoT replacement project last year. At Her Majesty's Prison and Probation Service, Kainos has helped design and implement the Assisted Prison Visits Scheme, which provides financial assistance to prisoners' close relatives or partners who visit them in prison. The Land Registry has engaged Kainos to work on the nationwide Local Land Charges programme to provide a central, digital service by consolidating local authority registers into a single register. Outside central government, the Group continues to work on digital projects for the Northern Ireland Civil Service, the National Assembly for Wales and the Scottish Courts and Tribunals Service.

There has been a high level of political uncertainty in the UK over the past two years, with a general election in May 2015, the 'Brexit' referendum in June 2016, the collapse of Northern Ireland political institutions in January 2017 and a further general election in June 2017. Despite this, the importance of the UK government's digitisation programme – and its support by the main political parties – has remained constant. Projects and contract signature have not been significantly delayed, and new programmes continue to be initiated, reflecting both the importance of the various departmental digitisation initiatives and the maturity of the market. As a result, the Group remains optimistic about the future of digitisation in the UK public sector, and is confident that it is well-positioned to maintain a central role in public sector transformation.

The implementation of the IR35 anti-tax avoidance reforms on 6 April 2017 is widely expected to reduce the number of independent IT contractors operating in the public sector. While there has been limited impact to date, the Group views this as broadly positive for Kainos, which operates an employee rather than a contractor model.

Digital Services – Workday Implementation
Kainos first engaged with Workday in 2010, deploying Workday's HCM platform at organisations such as Grant Thornton, EasyJet and Travelex, and is now one of the most experienced participants in Workday's partner ecosystem. Kainos remains the only boutique Workday partner headquartered in the UK and one of only 35 global partners accredited to implement Workday's innovative SaaS platform.

There has been further consolidation in the Workday partner ecosystem during the year ended 31 March 2017, with Appirio acquired by Wipro (October 2016) and DayNine acquired by Accenture (November 2016). The reduced competitive landscape in the boutique partner segment provides further growth opportunities for the Group.

Internationally, Kainos now provides Workday implementation services across mainland Europe, with offices in Amsterdam servicing customers in the Benelux region, and in Frankfurt (opened in March 2017 following the appointment of a regional director) servicing customers in Germany, Switzerland and Austria (DACH region). The Group is engaged in five significant Workday implementation projects across these two regions.

Workday segments its customers as Medium Enterprise (those with up to 3,000 employees) and Large Enterprise (those with more than 3,000 employees). The Group continues to win and deliver projects in both these segments, and has successfully deployed systems into live operation for Tullet Prebon (UK), Financial Times (UK), TomTom (Benelux) and United Drug Group plc (Ireland), with the latter project covering 7,500 employees across 16 countries.

The number of accredited Workday consultants in the Group's Digital Services division has increased by 47% to 110 people (2016: 75 people), with further recruitment anticipated over the course of 2018.

Looking forward, growth prospects remain very strong as Kainos extends its presence across Europe and the opportunity to establish the Workday platform in the UK Public Sector as a viable alternative to legacy 'on-premise' solutions. These prospects are underpinned by very strong revenue growth at Workday[4] and by reduced competition in the Workday ecosystem following consolidation in the boutique segment.

→ The Group has delivered good performance across all divisions, extended operations in Europe and the US and increased expenditure in research and development of its platform portfolio.

Digital Platforms
The Group Digital Platforms division comprises three discrete platforms:

- **Smart Automated Testing (Smart):** Smart is a proprietary software tool that allows Workday customers to automatically verify their Workday configuration. This SaaS platform is used during implementation projects, and to validate weekly updates of the live Workday platform for customers. Smart is the only automated testing platform available for the Workday product suite. Smart is a cloud-based SaaS solution licensed on a subscription basis to customers.
- **Evolve Electronic Medical Record (Evolve EMR):** Evolve EMR is a proprietary software product that removes paper from the care process by digitising patient records, thereby enabling efficient healthcare and supporting Digital Maturity programmes. EMR features in-built electronic forms and workflow that allows patient information to be captured and routed electronically, saving time and effort, and helping to improve quality of patient care. The Evolve EMR core product is sold to customers on a one-off perpetual licence basis, although a small number of Evolve EMR add-on modules are licensed on a subscription basis.
- **Evolve Integrated Care (Evolve IC):** Evolve IC is a mobile-optimised integrated care platform, designed to automate everyday care pathways for healthcare delivery organisations. It simplifies the provision of healthcare by integrating disparate healthcare systems and results in easier access, better outcomes and lower cost. Evolve IC is a cloud-based SaaS solution licensed on a subscription basis to customers.

4 Workday Fourth Quarter and Full Year Fiscal 2017 Financial Results which highlighted revenue growth of 35% to $1.57 billion.

Digital Platforms revenue (excluding third party revenue) for the year ended 31 March 2017 increased by 9% to £15.3 million (2016: £14.0 million). However, a decrease in third party revenue, which has a lower margin, meant that overall Digital Platforms revenue decreased by 12% to £19.0 million (2016: £21.5 million). Sales orders for Digital Platforms (excluding third party) decreased by 12% to £17 million (2016: £19.2 million), largely as a result of reduced order levels in the NHS. Sales orders for the Group's SaaS platforms increased by 17% to £10.1 million (2016: £8.6 million).

Digital Platforms – Smart

Smart is now used by 92 international customers to automatically verify their Workday configurations. Kainos has developed three Smart modules – HCM, Security and Financials – and a growing number of customers have subscribed to all three modules.

In the year ended 31 March 2017, the Group added 37 new Smart customers, including Blue Cross Blue Shield, Bristol-Myers Squib and GEICO. The increased level of activity in the US has resulted in expansion of the Smart presence in Los Angeles and Houston.

Smart revenue in the year ended 31 March 2017 increased by 96% to £4.7 million (2016: £2.4 million), of which £3.7 million relates to SaaS subscriptions. New sales in 2017 amounted to £9.2 million (2016: £6.1 million), an increase of 51%. The Annual Recurring Revenue (ARR) for Smart at 31 March 2017 is £5.5 million (2016: £2.5 million).

Looking forward, continued strong growth of Workday provides an opportunity to expand the pace and range of Smart successes in the coming year. There are opportunities to increase usage of all Smart modules across the Group's existing Smart customer base; similarly, there is an opportunity to develop additional modules to cover areas such as Payroll and Recruitment.

Digital Platforms – Evolve EMR

Evolve EMR continues to be a leading supplier to the NHS, and is now deployed at 35 Health Trusts in England, managing over 1.2 billion images and with 33 million patients registered on the system. During 2017, Colchester Hospital University NHS Foundation Trust became the latest NHS Trust to purchase Evolve EMR.

Funding for new technology in the NHS has remained limited despite an announcement from the Secretary of State for Health in February 2017 pledging over £4 billion to accelerate the adoption of digital solutions in the NHS. As a result, Evolve EMR revenue in the year ended 31 March 2017 (excluding third party revenue) decreased by 12% to £10.0 million (2016: £11.4 million). Sales orders in 2017 amounted to £4.8 million (2016: £9.9 million), a reduction of 52%; contracted backlog for Evolve EMR is £16.0 million (2016: £24.8 million).

Looking forward, the Group believes that the opportunity for Evolve EMR remains undiminished in the long term, with 98 Health Trusts in England still to purchase an EMR solution, representing an available market of approximately £200 million. However, it is likely that constrained technology funding in the NHS will persist in the near term, resulting in limited new procurements of Evolve EMR in 2018. During this period, the Group will seek to enhance the Evolve EMR product to meet the requirements of its existing customers.

Digital Platforms – Evolve IC

The Evolve IC platform was announced in February 2016 and is now operational in 38 US hospitals; it is also live at Cirdan Imaging Limited ('Cirdan'), a fast-growing medical diagnostics business. In 2017, a NHS Clinical Commissioning Group (CCG) signed a five-year subscription for Evolve IC as the central platform to integrate information from 11 different healthcare organisations.

Evolve IC revenue in the year ended 31 March 2017 was £0.6 million (2016: £0.03 million). New sales in 2017 amounted to £3.0 million (2016: £3.2 million), a decrease of 6%. (2016 performance was positively impacted by the signing of a landmark contract with US-based telehealth provider, InTouch Health).

Looking forward, the immediate priority is to support the NHS CCG and InTouch Health as they roll-out the Evolve IC platform. For InTouch Health, their network reaches a customer base of over 1,600 separate care locations across 130 individual Health Systems. In addition to the Stroke clinical workflow already in live use, workflows in the areas of Paediatrics, Cardiology, General Surgery, Neonatal Resuscitation, Dysphasia and Electroencephalogram (EEG) are currently under development for contracted customers.

Strategic Report continued

Key Performance Indicators (KPIs)

The Group aims to increase profitability while maintaining a healthy statement of financial position and investing in the operations and locations which underpin growth. It tracks a number of KPIs to identify trends in trading performance and to benchmark progress of key objectives, such as staff well-being and satisfaction. Financial KPI targets are used as a basis for remuneration awards, and are identified in the Directors' Remuneration Report.

Financial KPIs

Total sales orders
2017

£94.8m

2016

£87.2m

Revenue
2017

£83.5m

2016

£76.6m

Adjusted pre-tax profit
2017

£14.3m

2016

£14.1m

Non-financial KPIs

Overall customer satisfaction rating[5]
2017

92%

2016

97%

Number of customers
2017

247

2016

209

'Best Companies to Work For' ranking
2017

44th

2016

37th

Staff attrition
2017

8%

2016

10%

5 Data collated from regular feedback surveys conducted with sub-set of Kainos customers over the course of the year.

Risk factors and uncertainties

There are a number of potential risks and uncertainties which could have a material impact on the Group's operations, its financial results or the value and liquidity of its securities, and could cause actual results to differ materially from forecast and historic results.

The following table identifies the principal risk factors but may not be exhaustive. There may also be risks that are not currently considered to be serious or which are currently unknown, and risks that are outside of the Group's control. Where reasonably possible, Kainos has taken steps to mitigate the risks or potential risks but it cannot entirely safeguard against all of them.

Risk factor	Risk	Risk mitigation
Financial	• Financial or trading risks associated with the UK leaving the European Union.	• The Group has evaluated scenarios associated with 'Brexit' and concluded that there is no substantial risk to operations in the next two to three years. The Group is not overly reliant on UK-EU trade (its most significant customers are UK public sector organisations). Operations in the Group's Polish subsidiary are predominantly focused on product development and are largely independent of UK labour or trade restrictions.
Reputational	• Failure of software products or undetected faults in the Group's software platforms or software developed for customers.	• Kainos implements a portfolio of quality assurance checks that reduce the likelihood of failure of client projects. Development of Kainos proprietary software is subject to robust quality control at every stage of the development and test life cycle.
	• Unauthorised access to Group data or to customer data that is held or managed by the Group, or exposure to other forms of malware or cyberattack.	• Kainos is aware of the increasing risk of cybercrime and has implemented a robust defence against cyberattacks, including the deployment of malware or unauthorised access to data. These measures include such controls as Authenticated User Access, Firewalls, Network Access Protection, Anti-Virus Protection, Encryption, Pro-active Threat Analysis and User Education. The Group has also achieved ISO27001 certification of its technical infrastructure, including network security.
	• Third party scanning errors and clinical safety risks.	• Kainos has a rigorous selection and quality process for third party scanning partners. This is regularly monitored and any partner deemed at risk, or that fails to perform to the satisfaction of the Group or the customer, is not reselected for work with Kainos. • Kainos has appointed a clinical safety officer to work with its healthcare customers on compliance with relevant NHS guidance and standards on clinical safety and where appropriate seeks external consultancy and advice.
	• Negative associations with Kainos and subsidiary brands.	• Kainos actively monitors press, online and social media channels to ensure that it identifies potential reputational or defamatory risk. In conjunction with its advisers, it has developed a proactive approach to addressing any negative associations in the public eye.
	• Loss of reputation due to employee behaviour.	• Kainos publishes and promotes a best practice policy for use of social media and public channels by employees, which is designed to minimise the potential for deliberate or accidental negative publicity for the Group.

Strategic Report continued

Risk factor	Risk	Risk mitigation
Infrastructure	• Loss of key employees, or inability to recruit sufficiently qualified employees in core markets and locations.	• Kainos has worked to become an employer of choice in certain of its key locations, notably Belfast and Gdansk, and has implemented a team, processes and infrastructure dedicated to recruiting the most appropriate candidates in a streamlined hiring process.
	• Inadequate succession planning.	• Kainos has developed a succession plan that addresses succession for senior management (including divisional management teams) in the case of unforeseen events, and also from the point of view of career progression for up and coming leaders.
	• Unauthorised access to and/or sabotage of systems, including unauthorised access resulting in loss or corruption of customer data held or maintained by the Group.	• Kainos has robust information and physical security policies and procedures which provide a reasonable level of protection against sabotage. They also limit access to systems, office and data centre areas to appropriate personnel. Penetration and security testing is undertaken to monitor the effectiveness of security and identify areas for improvement.
Marketplace	• Claims for infringement of a third party's intellectual property or infringement of the Group's intellectual property.	• Kainos enters into non-disclosure agreements with employees, independent contractors and third parties in the ordinary course of its business to provide a degree of protection to its intellectual property, domain knowledge and know-how. Where practical, focused patent searches are undertaken to identify areas that new products or services under development may conflict with third party patents.
	• Removal of access to essential intellectual property or partnership.	• Kainos has entered into contracts with its main partners, Workday and Apple, to secure access to proprietary materials including code, know-how and branding which the Group needs to deliver or enhance its services.
	• Failure to be selected on public procurement frameworks.	• Kainos' divisions that are engaged in public sector procurement actively review all existing and renewed government procurement frameworks. The Group has built specific pre-sales expertise that enables it to compete effectively in public procurement competitions.
	• Contractual failure.	• Kainos maintains a rigorous process for approving contractual terms and deliverables to control the level of risk that is accepted.

Employees and career development

The directors believe that investment in people is key to helping the Group achieve its ambitions. This is considered a priority, and a member of the executive team is dedicated to overseeing all aspects of staff recruitment, career development and progression. To complement this role, this year Kainos appointed its first dedicated Group Chief Information Officer (CIO), responsible for ensuring the quality, security and availability of the Group's technical infrastructure and information assets.

Kainos staff continue to set new standards of quality and achievement. This year, publicity surrounding the award of the prestigious 'Entrepreneur of the Year' to Group CEO Brendan Mooney resulted in considerable interest in the Group as an attractive place to work. In Gdansk, the scale of our operation continues to distinguish the Group as a premier digital employer in Poland and the surrounding area. Following the successful establishment of a Kainos office in Amsterdam, Netherlands in 2015, the Group opened a new office in Frankfurt, Germany in February 2017. Key recruits in the US this year include a regional head of sales for the Evolve Integrated Care platform, and this brings the number of Kainos staff in the US to five at year end.

The average number of employees at Kainos during the year was 884, up from 733 last year, and the number of employees (including contractors) at 31 March 2017 was 975 (2016: 840). Recruitment remained a priority during the year, with 216 new staff joining the Company over the period. In Gdansk, the product development centre for the Group, 60 new jobs were created.

In parallel, the Group extended its MAP (Master, Accomplish, Progress) academy, which provides on-boarding, career development and training for Kainos staff in all locations. Over 180 staff have already benefited from attending the new Apprentice, Trainee, Consultant and Management level programmes that form MAP.

The Group continues to expand its popular Earn as You Learn® apprenticeship scheme, which has proven particularly successful since its inception in 2013. Designed to encourage young people into the digital industry, Earn as You Learn has allowed the Group to identify talent outside its traditional graduate recruitment pools. There are now 30 Earn as You Learn recruits employed in Kainos, all of whom have been successfully integrated into operating Divisions. It is expected that the scheme will expand further in the coming years to take advantage of the UK government's Apprentice Levy scheme.

Once again, the Group was pleased to achieve a top 50 position in the prestigious Sunday Times 'Best Companies to Work For' programme, achieving 44th place in February 2017. This strong showing reflects the increasing investment the Group is making in career development of its staff, and highlights the value of ancillary well-being initiatives, such as the Skills for Me programme, which offers £250 each year to employees to develop talents outside the workplace.

Looking forward, the pace of recruitment and training is expected to remain strong, both in the Group's development centres in Belfast and Gdansk and in increasingly international regional offices. Attrition levels remained well below the industry average, at 8% (2016: 10%), despite increased competition for talent in some locations, notably London and Dublin. Attrition in the Group's main development centre in Northern Ireland improved to 4% (2016: 5%).

Diversity, equal opportunity and human rights

Kainos has an obligation to all staff and the wider community to respect and uphold people's basic human rights. The Group firmly believes that continued success depends on attracting, developing and retaining the best staff, and nurturing their potential to the full. It also recognises that maintaining a competitive edge requires a highly skilled, competent, flexible and motivated workforce. Accordingly, the Group's employment policy encourages a productive working environment which helps all employees to develop their full potential, and allows Kainos to make full use of the talents and resources of its staff. Kainos is committed to being an inclusive and fair employer and to creating equal opportunity for employees regardless of colour, nationality, sex, marital status, sexual orientation, age, religion, disability or any other characteristic protected by law. Applications for employment by disabled persons are always fully considered, bearing in mind the aptitudes of the applicant concerned. Wherever possible the employment of staff who become disabled will be continued and appropriate training and career development will be offered.

Gender diversity remains a challenge in an industry that is predominantly male. In an effort to redress this imbalance, the Group actively seeks to recruit women, and has participated in various initiatives designed to promote the role of women in technology, such as Women Who Code. This has had some success: at 31 March 2017, the number of women employed by Kainos was 254 (approximately 26% of the total workforce), a figure well above the 17% level for the UK ICT industry as a whole.

	Male	Female
Directors	4	–
Senior managers (executives)	7	2
Other employees	710	252

The Group also looks to encourage a wider range of ethnicities and the increasing diversity of background means that today the Group employs staff with over 10 different nationalities. The Group does not tolerate any slavery or human trafficking in any part of its business operations and takes a risk-based approach regarding its supply chains.

Corporate social responsibility

The Group views it as part of its mission to promote awareness of digital technologies amongst school leavers and young people. This has the benefit not only of growing the pool of talent available to industry where Kainos has a presence, but also of positioning Kainos as a socially-aware and responsible organisation. In this regard, the Group can justly claim a unique position as mentor to generations of information technology specialists. The ability to shape talent prompted Kainos to set up its Digital Academy, a range of initiatives designed to encourage digital talent into the UK workforce, and to align all Group corporate social activities under a dedicated Tech Outreach function.

Under this umbrella, Kainos has run 'hackathons', coding camps, and innovative work placements for young people to get them excited about digital technology, and these activities have proved as rewarding for staff as for the participants. Kainos Tech Outreach has been successful at inspiring children, empowering teachers and influencing policy makers to improve digital literacy. Tech Outreach has also helped co-ordinate the 'Time off for Volunteering' initiative, which offers a fixed term of paid leave to any employee who wishes to volunteer for a charity of their choice.

Customer satisfaction and quality

In recent years the Group has created a streamlined mechanism to capture high-level customer feedback on client engagements with the intent of measuring quality and identifying where improvements could be made. This comprises a concise online questionnaire delivered via a professional and modern interface that allows customers to submit feedback at any stage during an engagement. Data gathered in this way is submitted to an in-house Services Management solution and used to track and present key metrics in an easy to digest dashboard format.

Feedback is captured for quality of solution, services and people. In 2017, 77 customer engagement surveys were received. All three categories were rated as 'Good or Above' by over 90% of customers ('People' – 97%; 'Services' – 95%; 'Solution' – 90%). An overall feedback rating is also measured, and in 2017 92% of responses gave Kainos an overall rating of 'Good or Above'.

The Group uses these statistics to inform its continuous improvement programme, which is designed to meet and often exceed customer expectations on every engagement.

Research and development

In 2017, the Kainos Chief Technology Officer (CTO) was appointed as CEO of the Northern Ireland branch of Digital Catapult, a UK-wide organisation that promotes innovation and digital awareness. This increased significantly the profile of the Group's research and development function, which has continued to drive thought leadership amongst customers and partners. Once again this year, the Kainos R&D team was included in the prestigious South by South West conference (SXSW Interactive) in Austin, Texas; and in April 2016, Kainos curated the now well-established annual Beltech technology conference, showcasing local and international digital entrepreneurship, and inspiring the next generation of digital leaders.

Looking forward, the research focus will continue to be on Machine Learning and the Internet of Things (IOT), independently and in conjunction with partners and where possible, with customers. This will be supplemented by increased visibility at key industry events and partnership with like-minded innovative organisations to identify opportunities for product and offering synergy.

Environment

Kainos understands the importance of meeting globally recognised corporate responsibility standards. It encourages its employees and suppliers to act in an environmentally responsible manner and it has endeavoured to manage the effect that it has on the environment and to support sustainability.

As a software product and services office-based provider, Kainos has no activities that pose major environmental issues. Usage of energy to facilitate the computing requirements of its data servers and its employees, as well as international travel, are considered to be the greatest environmental impacts associated with its daily operations. Other factors include the use of electrical and electronic equipment, the consumption of water, the use of paper and the disposal of waste.

Kainos endeavours to minimise energy and natural resource usage, support the reduction and recycling of materials and ensure the legal disposal of waste arising from the activities of the business. Kainos encourages employees to reduce their usage of those resources and sets policies and procedures to assist in this so that productivity is not negatively impacted.

In accordance with regulation, Kainos is required to make certain disclosures concerning greenhouse gas emissions relating to the current and preceding financial years. For the year ended 31 March 2017 the quantity of Scope 2 emissions by Kainos was 442.9 tonnes of carbon dioxide equivalent (CO_2e), (2016: 395.4 tonnes).

The GHG Protocol Corporate Accounting and Reporting standard (revised edition) and emission factors from the UK government's GHG Conversion Factors Guidance 2013 were used to calculate the quantity of emissions. The standard requires a statement of relevant intensity ratios, which are an expression of the quantity of emissions in relation to a quantifiable factor of the business activity. Kainos has identified four such intensity ratios, set out below. These figures were calculated from data available for the Group's main operations and extrapolated to take account of its smaller locations. Scope 1 data has not been included as it is not considered to be material.

Intensity ratios (tonnes of CO_2e per unit)

Ratios of carbon emissions to:

	2017	2016
Total revenue	**0.01**	0.01
Recurring revenue	**0.01**	0.01
Operating profit	**0.03**	0.03
Employees	**0.45**	0.65

The Strategic Report was approved by the Board and signed on its behalf by:

Brendan Mooney
Chief Executive Officer
26 May 2017

Directors' and Corporate Governance Report

This section of the Annual Report outlines how the Board maintains high standards of corporate governance as well as providing a summary of how each of the Board's Committees function. This includes detailed Directors' Remuneration, Nominations Committee and Audit Committee reports.

The Board believes in good governance and recognises the importance of complying with the various aspects of the UK governance framework. Crucial to good governance is a stable Board that contains the right balance of skills and experience; therefore, Board appointments are taken very seriously.

The Board continues to welcome interaction with shareholders and I and the other NEDs are available for dialogue as an alternative to meetings with the Executive Directors.

Dr John Lillywhite
Chairman

The directors present their report and the audited financial statements for Kainos Group plc (company number 9579188) for the year ended 31 March 2017. These will be laid before the shareholders at the Annual General Meeting (AGM) to be held on 28 September 2017. The Strategic Report is incorporated by reference into this Directors' Report.

All sections of the Annual Report contain certain forward looking statements which by their nature involve risk and uncertainty. The forward looking statements are based on the knowledge and information available at the date of preparation and on what are believed to be reasonable judgements. A wide range of factors may cause the actual results to differ materially from those contained within, or implied by, these forward looking statements. The forward looking statements should not be construed as a profit forecast.

Directors

The Board currently comprises a Chairman, three Independent NEDs and three Executive Directors.
The serving directors are:

Dr. John Lillywhite (aged 76) Chairman
John is a Fellow of the Institute of Management Accountants and has been in the Information Technology industry for over 50 years. In 1997 he stepped down as Group Finance Director of ICL (now Fujitsu Services) after a long career with the Group in which he worked in the UK, Europe, US and the Far East filling roles in divisional management and various aspects of finance, including group CFO where he was responsible for acquisitions, disposals, start-ups and recovery programmes. In 2011 he was awarded an Honorary Doctorate from Queen's University, Belfast for services to commerce and industry. John has been Chairman of seven start-up companies and is a trustee director for a large pension fund. John acts as a Non-Independent Non-Executive Chairman, sits on the Audit Committee and Remuneration Committee and chairs the Nominations Committee.

Dr. Brendan Mooney (aged 50) Chief Executive Officer (CEO)
Brendan joined Kainos in 1989 as a graduate software engineer before moving into a number of technical and commercial roles in Dublin, London and the US. He was appointed CEO of Kainos in 2001. In addition to his role at Kainos, Brendan has been a NED at Meridio, Property News, the Probation Service for Northern Ireland and, until recently, was a serving Lay Magistrate. Brendan is the recipient of an Honorary Doctor of Science (DSc) in recognition of his services to business development. As CEO, Brendan is responsible for setting the strategic direction of the Group and for overseeing its profitable growth.

Richard McCann (aged 52) Chief Financial Officer (CFO)/Chief Operating Officer (COO)
Richard is a Fellow of the Institute of Chartered Accountants in Ireland and trained with Coopers & Lybrand, before moving into industry with Galen Holdings plc. Richard joined Galen as financial controller of a start-up subsidiary in the US and subsequently became Senior Vice President in charge of Corporate Finance with responsibility for the organisation's acquisitions and investor relations. He served as the Managing Director of two subsidiaries in the Almac Group, including a US subsidiary that provides software development services for pharmaceutical companies. Richard joined Kainos in 2011, with over 20 years' experience in accounting and serves as the Chief Financial Officer and Chief Operating Officer.

Paul Gannon (aged 54) Senior Vice President (SVP) Business Development
Paul studied Engineering at Trinity College, Dublin. Before joining Kainos, Paul spent four years in a sales role with ICL (now Fujitsu) in Dublin and prior to that worked as a management consultant for Accenture in London. He started his professional career working for Siemens in Munich. He joined Kainos in 1998 as the sales manager for Ireland. Paul subsequently took on a Group-wide role in strategy and marketing, and until March 31 2017 was SVP Sales, responsible for all product and service sales activities in Kainos. He is currently the SVP Business Development at Kainos, responsible for identifying new markets and opportunities for the Group.

Andy Malpass (aged 55) Independent Non-Executive Director
Andy graduated with a BA (Hons) in Accounting and Finance from Lancaster University and is a Fellow of the Chartered Institute of Management Accountants. He has over 30 years' experience in the software industry covering both private and public companies. Most recently, Andy served as Group Finance Director of Fidessa Group plc (formerly Royalblue Group plc) which he joined in 1995, and where he has also been Company Secretary. Andy acts as Senior Independent NED and chairs the Audit Committee.

Chris Cowan (aged 58) Independent Non-Executive Director
Chris holds an MA History from St Catharine's College, Cambridge. Chris runs a board advisory business focused on digital transformation and has previously served as Managing Director of Accenture's Telco, Media and Technology business in the UK; Accenture's Telco Industry Managing Director for EMEA; Chairman and CEO of Digiplug (an Accenture Digital business); and Managing Director of Value Partners Group's UK business. Chris acts as an Independent NED and sits on the Audit Committee, Nominations Committee and Remuneration Committee.

Tom Burnet (aged 49) Independent Non-Executive Director
Tom graduated with an MBA from the University of Edinburgh. Tom was previously CEO and is now Executive Chairperson of AIM company Accesso Technology Group plc, a leading supplier of technology platforms to the global leisure and attractions market, serving over 1,000 customers in 27 countries. Previously he was Managing Director of Serco's Defence Services division and Managing Director of QinetiQ's consultancy business. He started his career as the UK's youngest Army Officer serving in the Black Watch (R.H.R.) and is a member of the Queen's Bodyguard in Scotland. Tom acts as an Independent NED; he sits on the Nominations Committee and chairs the Remuneration Committee.

The Board considers its overall size and composition to be appropriate, having regard to the experience and skills which the Board members bring together. When reaching its decision, the Board considered the independence criteria set out in paragraph B.1.1 of the Code. By virtue of their recent appointment and given the due diligence carried out on their independence, the Board confirmed that Andy Malpass, Chris Cowan and Tom Burnet are independent in character and judgement. The Chairman, John Lillywhite, does not meet the independence criteria set out in the Code. The Board considers that John Lillywhite's long experience as Chairman of the Board of Kainos Software Limited (which, prior to the IPO, was the parent company of the Group) will be of benefit to the Board in providing continuity of knowledge of the Group. John Lillywhite intends to remain as Chairman of the Board in the medium term, and the Group will consider the appointment of a Deputy Chairman next year.

The Chairman confirms that, as supported by the results of the 2017 Board Evaluation exercise undertaken by the Nominations Committee, the performance of each of the directors continues to be effective and that they continue to demonstrate commitment to their roles, bringing their considerable commercial experience to Kainos.

The Senior Independent Director (SID), Andy Malpass, confirms that, as supported by the results of the 2017 Board Evaluation exercise, the performance of the Chairman continues to be effective.

Directors' interests in shares and share incentives in Kainos Group plc are detailed in the Directors' Remuneration Report.

At the date of this Directors' and Corporate Governance Report, indemnities are in force under which Kainos has agreed to indemnify the directors and the Company Secretary to the extent permitted by law and by Kainos Group plc's Articles of Association in respect of losses arising in their capacity as officer of any member of the Kainos Group. In addition, Kainos has purchased and maintained throughout the year directors' and officers' liability insurance in respect of itself and its directors and officers.

The Board

At 31 March 2017 the Board comprised the Chairman, three Executive Directors and three NEDs whose Board and Committee responsibilities are set out in the table below:

		Board	Audit Committee	Remuneration Committee	Nominations Committee
John Lillywhite	Chairman	Chairman	Member	Member	Chairman
Brendan Mooney	CEO	Member	–	–	–
Richard McCann	CFO/COO	Member	–	–	–
Paul Gannon	SVP Sales	Member	–	–	–
Andy Malpass	Senior Independent NED	Member	Chairman	–	–
Chris Cowan	Independent NED	Member	Member	Member	Member
Tom Burnet	Independent NED	Member	–	Chairman	Member

The Board meets formally on a regular basis to monitor operating issues, risk and trading performance, to review forecasts, strategy and policy, to consider key projects and major investments and to oversee appropriate shareholder reporting. The Board is responsible for corporate governance and delegates operational control to the Executive Directors. During the year, the Board met on ten scheduled occasions for this purpose. In addition, if required, impromptu Board meetings occur to consider specific issues as and when necessary. Meetings were held by the Chairman with the NEDs, without the Executive Directors present, to discuss the performance of the Executive Directors.

The Chairman and NEDs also held meetings throughout the year with various senior managers to improve insight into the business operations and marketplace. The attendance of individual directors at Board meetings and Committee meetings is presented in the table below:

	Board meetings attended	Audit Committee meetings attended	Remuneration Committee meetings attended	Nominations Committee meetings attended
John Lillywhite	10/10	2/2	6/6	3/3
Brendan Mooney	10/10	–	–	–
Richard McCann	10/10	–	–	–
Paul Gannon	9/10	–	–	–
Andy Malpass	10/10	2/2	–	–
Chris Cowan	10/10	2/2	6/6	3/3
Tom Burnet	10/10	–	6/6	2/3

Absences were due to prior commitments.

There is a formal schedule of matters reserved for the decision of the Board that covers key areas of Kainos' affairs. The schedule includes approval of the Annual Report and any other financial statements, the adoption of budgets or business plans, decisions on acquisitions and disposals, material financial commitments and the release of inside information. Certain matters require Board approval and other matters may be approved by senior management, but notification to the Board is required. The schedule of matters reserved for the Board is reviewed annually. A procedure exists to allow the directors to seek independent legal advice in respect of their duties at Kainos' expense where the circumstances are appropriate. All directors have access to the Company Secretary for her advice and services.

There was a formal evaluation of the performance of the Board during 2017. This consisted of an internally run review conducted by the Chairman with the Company Secretary. The performance evaluation questionnaire was based on the Code process and it covered the areas of Board structure, effectiveness, Committees, information and communication. Questionnaires were completed by the directors and submitted for discussion. The feedback generated from the questionnaires was discussed by the Board, together with potential improvements that could be made. The conclusion was reached that the Board is operating effectively. An evaluation of the Chairman by the NEDs without the Executive Directors present was also carried out and it was concluded that he was performing his role effectively. In accordance with the requirements of paragraph B.6.2 of the Code, the next independent evaluation of the Board's performance is scheduled to be conducted in 2018.

There is a formal written policy on the division of responsibilities between the Chairman and the CEO such that their roles are complementary to each other. John Lillywhite as Chairman is principally responsible for leading the Board, promoting constructive debate amongst the Board and facilitating communication with shareholders as well as overseeing strategy. Brendan Mooney as CEO is responsible for all aspects of Kainos' operations; he leads and develops the strategic plans for the business and identifies risk factors.

Directors undergo a thorough, formal and tailored induction process on joining and, following regular reviews by the Chairman of training and development requirements, receive ongoing updates to improve their skills and knowledge according to their personal and external needs. The Company Secretary is responsible for advising the Board and updating it on governance and regulatory matters.

The Companies Act 2006 imposes a statutory duty on directors to avoid conflicts of interest. The Articles of Association allow the directors to consider and, if they deem fit, to authorise conflicts of interest. The Articles of Association set out the process for authorisation of such conflicts and any such conflicts will be recorded in the Board minutes and maintained on a register which will be reviewed on an annual basis by the Nominations Committee and by the Board.

No conflicts have arisen in the year ended 31 March 2017.

The Directors' and Corporate Governance Report was approved by the Board and signed on its behalf by:

Grainne Burns
Company Secretary
26 May 2017

Committees of the Board
The constitution and responsibilities of the Board's Committees are set out below.

Directors' Remuneration Report

Statement from the Chairman of the Remuneration Committee
As Chairman of the Remuneration Committee I am pleased to introduce the Directors' Remuneration Report for the year ended 31 March 2017.

Introduction
This is the Company's second Annual Report since its admission to the Official List of the London Stock Exchange in July 2015. I was appointed Chairman of the Remuneration Committee at the time of the Listing and my fellow members of the Committee, Chris Cowan and John Lillywhite, were appointed at the same time.

This report by the Remuneration Committee has been approved by the Board for submission to shareholders in accordance with the UK Corporate Governance Code, the requirements of the Listing Rules of the UK Listing Authority and the reporting requirements of The Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013 (the Regulations).

The report has been split into two sections: the Directors' Remuneration Policy, which sets out the policy on the remuneration of the Executive Directors and NEDs, and an Annual Report on Remuneration, which discloses the directors' remuneration for the year ended 31 March 2017. The policy was put to a vote at the 2016 AGM, and I was delighted that the policy was strongly supported by shareholders, with over 99% of votes cast in favour. The Remuneration Committee will keep the policy under review to ensure that it remains appropriate to the delivery of long term value for all stakeholders. The policy is set out below and took effect from the 2016 AGM, although in practice was applied throughout the year. Overall, the Remuneration Committee believes that the policy remains appropriate and, accordingly, it has decided not to make any changes for 2017.

Link between remuneration and strategy
The strategy of the Group is to achieve sustained revenue, profit and cash flow growth in its chosen markets. The Remuneration Committee is committed to continue structuring executive remuneration to fit the Group's business model and support its strategy. Overall packages are set at attractive levels to retain and motivate executives with a significant portion based on performance. Salaries are kept at below median levels compared to peer companies. Short term performance is incentivised via an annual bonus which is currently based on revenue, adjusted pre-tax profit and sales order value targets and paid in cash. Long term performance is incentivised via a share plan under which executives are awarded performance shares subject to achieving Total Shareholder Return (TSR) and Earnings per Share (EPS) growth over a three year period.

The Board has applied a policy of using share incentives extensively across the Group. The Board regards this as an important principle aligning all employees with shareholders and allowing them the potential to benefit from the Group's success. This includes Company Share Option Plan (CSOP) awards to more senior staff, excluding executives, and awards under both Save As You Earn (SAYE) and Share Incentive Plan (SIP) across the Group, including executives.

Performance and decisions taken on remuneration in 2016/17
The CEO's statement earlier in this Annual Report provides a summary of the progress the Group has made in the year ended 31 March 2017. In summary, the Group has delivered good performance across all divisions, extended operations in Europe and the US and increased expenditure in research and development of its platform portfolio. Key performance indicators are solid across the Group: revenue increased from £76.6 million to £83.5 million, adjusted profit before tax increased from £14.1 million to £14.3 million, and sales orders increased from £87.2 million to £94.8 million. The Group continues to attract high quality talent, and is pleased to note that the number of staff at year end was almost 1,000 across eight offices in the US and Europe.

Performance against the adjusted pre-tax profit target was ahead of target with performance against the revenue and sales order value targets being between threshold and target. As a result, bonuses paid to the CEO, CFO and Sales Director were 69%, 67% and 114% of salary, respectively.

In June 2016, the Company made performance share awards to the CEO, CFO and Sales Director at 40%, 50% and 40% of salary, respectively.

No long term incentive awards were due to vest during the year and none vested.

Implementation of policy for 2017/18
For the current financial year, ending 31 March 2018, the Group is not proposing any material change to the remuneration arrangements that are already in place.

The salaries of the CEO and CFO effective 1 April 2017 are unchanged from the previous year. From 1 April 2017, Paul Gannon's role changed from SVP Sales to SVP Business Development and he relocated to Dublin. His salary will be €243,000 having previously been £195,000.

For 2017/18, the normal on target and maximum annual bonus levels are 82% and 123% for the CEO, 79% and 119% for the CFO and 126% and 190% for the SVP Business Development.

The Remuneration Committee intends to make further performance share awards to the Executive Directors in mid-2017.

Directors' remuneration policy

Set out below is a copy of the policy which was approved by shareholders at the 2016 AGM, held on 22 September 2016.

The Group's remuneration policy seeks to ensure that the Group is able to attract, retain and motivate its executives and senior management. The Remuneration Committee believes that the Executive Directors and senior managers should be rewarded fairly and competitively according to their performance. Overall, this should be at a comparable level to directors in similar companies and at a level that will attract, motivate and retain individuals of an appropriate calibre to deliver the Group's strategy and value to shareholders.

The Group's executive remuneration philosophy is that salaries should remain lean and that a significant proportion of the remuneration of the Executive Directors and senior management should be performance-related, so that management is clearly focused on financial performance. While the annual bonus is focused on revenue, adjusted pre-tax profit and sales order value in the year, the long term share-based incentives are focused on earnings per share and share price performance measured over many years. The focus on financial performance and shareholder return encourages consistent performance over multiple years and aligns remuneration with the Kainos strategy and shareholders' interests. It aims to deliver value and good growth over the long term while striking an appropriate balance between caution and risk.

The Remuneration Committee is directly responsible for setting the remuneration of Executive Directors, giving guidance on the remuneration of other members of the senior management team and supervising the workings of all the Company's share incentive plans.

The individual elements of the remuneration packages offered to Executive Directors are set out in the table below.

Key elements of remuneration

Element	Purpose	Operation	Potential remuneration	Performance metrics
Base salary	To attract and retain executives	Reviewed annually in April and fixed for 12 months, commencing 1 April each year. The Remuneration Committee takes into account: • an individual's experience, knowledge and performance in the role • business and individual performance • achievement of objectives • comparative salaries and periodic reviews • the Group's financial position • the salary increases being provided to Kainos employees.	Percentage increases will normally be in line with other employees in the same location. Higher increases may be awarded in certain circumstances if there are commercial reasons for doing so such as to reflect market movements, changes in job responsibilities and to address retention issues.	None
Benefits	To attract and retain executives	The Executive Directors are entitled to a car allowance, private medical insurance, life insurance and permanent health insurance.	No maximum is set but the Remuneration Committee will monitor the overall cost of the benefits package. Any changes will normally be in line with other employees in the same location.	None

Key elements of remuneration continued

Element	Purpose	Operation	Potential remuneration	Performance metrics
Pension	To attract and retain executives	The Executive Directors are entitled to participate in the Group's pension scheme or receive a payment in lieu of pension.	The maximum payment by the Group is set at 15% of salary. The CEO and CFO currently receive payments in lieu of pension of 8.6% and 5% of salary, respectively. The SVP Business Development participates in the Group's pension scheme and receives a Group contribution of 15% of salary.	None
Annual bonus	To reward and incentivise performance within a financial year with adequate reward for good performance and excellent reward for exceptional performance, to focus executives on key objectives and support positive team behaviour	Performance is measured on an annual basis for each financial year. Criteria are established and weighted at the beginning of each year based on Group financial targets. Threshold and target levels of performance are determined for each criterion. At the end of the year, the Remuneration Committee determines the extent to which targets were achieved. On target levels of payment are set for each Executive Director at the start of each year. Up to 150% of these levels may be paid where targets are exceeded based on the extent to which the target is exceeded. Annual bonus is normally paid in cash following the completion of the audit of that year's financial statements. Annual bonus is subject to clawback provisions (net of any irrecoverable tax) for up to two years in the event of misstatement of financial information. Payments may be deferred for up to three years and then paid in cash or in shares. The Remuneration Committee has discretion to apply 'corporate override' in the event core targets are not achieved or in the event of a material negative event.	The maximum annual bonus opportunity under the policy as a percentage of the Executive's salary is 150% for the CEO, 150% for the CFO and 225% for the SVP Business Development. For 2017-18 the current normal on target and maximum annual bonus levels are 82% and 123% of salary for the CEO, 79% and 119% of salary for the CFO and 126% and 190% for the SVP Business Development.	Annual bonus is discretionary. Criteria are chosen, weighted and targets set each year by the Remuneration Committee in accordance with business priorities. For the year to March 2017, the targets included measures for revenue, adjusted pre-tax profit and sales order value. An element of the bonus may also be based on personal performance.

Key elements of remuneration continued

Element	Purpose	Operation	Potential remuneration	Performance metrics
Long term incentive plan (LTIP)	To motivate executives, incentivise performance over the long term and to facilitate share ownership	Performance share awards are made under the Group's 2015 Performance Share Plan (PSP). Awards, made in the form of nil or nominal cost options, normally vest at least three years following the date of award subject to continued employment and the meeting of appropriately challenging performance conditions specified at the outset. The Remuneration Committee determines the extent to which performance conditions have been met. Awards may be increased for dividends paid during the period. The Remuneration Committee determines the performance conditions, weighting and target performance levels at the point of award. Initial awards were made at the time of the IPO and will vest during the financial year ending 31 March 2019. Clawback may be applied at the discretion of the Remuneration Committee in the event of material misstatement of the financial results or if other exceptional circumstances exist such as gross misconduct.	The normal maximum level of annual award is 200% of salary. In exceptional circumstances, awards may be made up to a maximum of 300% of salary. In the event of a new appointment the Remuneration Committee would expect to make a higher award, closer to the normal maximum. 30% of awards vest at threshold levels of performance.	For the award at the time of IPO, 50% was linked to growth in adjusted EPS and 50% linked to total shareholder return. For future awards, the Remuneration Committee will assess what measures and targets best support the long term focus of the Group and so measures and targets may be different from year to year.
Policy for other employee incentive arrangements				
Share options	To motivate and facilitate share ownership	Market value options may be granted to employees at the discretion of the Remuneration Committee under the 2015 Performance Share Plan. UK employees may receive tax advantaged awards under the CSOP Sub-Plan. Options have a market value exercise price and have a normal minimum vesting period of three years. At the time of the IPO, options were granted to certain managers and employees, not Executive Directors.	It is not intended to grant CSOP options to Executive Directors.	Performance conditions may be applied but it is intended that CSOP options will not normally have performance conditions attached.

Key elements of remuneration continued

Policy for other employee incentive arrangements continued

Element	Purpose	Operation	Potential remuneration	Performance metrics
Save As You Earn Option Plan (SAYE)	To motivate, facilitate share ownership and align employees with shareholders	An 'all employee' share option plan approved by HMRC, supervised by the Remuneration Committee. UK Employees, including Executive Directors, may enter into a savings contract under which they agree to save a specified monthly amount for three or five years. At the end of the contract period, participating employees may use the amount saved to exercise options with an exercise price of up to a 20% discount to the market price at the outset. The Board shall determine if and when further SAYE awards will be made and the terms of SAYE participation.	Under the plan, the maximum monthly savings amount is £500. At the time of IPO, UK employees were offered participation with a maximum monthly savings limit of £100.	None
Share Incentive plan (SIP)	To motivate, facilitate share ownership and align employees with shareholders	An 'all employee' share option plan approved by HMRC, supervised by the Remuneration Committee. Significant tax advantages apply if shares acquired under the plan are held for five years. UK Employees, including Executive Directors, may be awarded free shares up to a maximum value of £3,600 each year. They may purchase partnership shares out of pre-tax salary up to £1,800 per tax year and may be awarded up to two free matching shares for each partnership share acquired (although no matching was implemented for Kainos 2015 SIP awards). The Board shall determine if and when further SIP awards will be made and the terms of those awards.	At the time of IPO, free shares with a value of between £1,000 and £3,600 were awarded to UK employees, including Executive Directors, depending on their length of service.	None

Key elements of remuneration continued

Element	Purpose	Operation	Potential remuneration	Performance metrics
Policy for other employee incentive arrangements continued				
Poland and Ireland Share Schemes	To motivate, facilitate share ownership and align employees with shareholders	The Group has implemented share schemes for employees in Poland and the Republic of Ireland with the intention of making share awards to these employees on similar terms and of a similar value to those made under the UK SAYE and SIP schemes.	Employees based in these countries may be awarded participation in these plans at similar levels of that offered to UK employees under the SAYE and SIP schemes. If Executive Directors were based in these countries, they would be able to participate in these schemes.	None
NED remuneration				
Chairman and NEDs	To attract and retain NEDs with appropriate experience and skills	The Chairman and NED remuneration comprises only fees. The Chairman's fee is approved by the Board on recommendation of the Remuneration Committee (with the Chairman who is a member of the Remuneration Committee recusing himself). Fees for the NEDs are approved by the Board on the recommendation of the Chairman and Executive Directors. Additional fees, over and above the base fee for the NEDs, are payable to the Chairmen of the Audit and Remuneration Committees and to the SID. Additional fees are paid in the event the time requirement is above normal levels.	The fees of the NEDs are reviewed annually taking into consideration the time commitment and responsibilities of the role and fees paid in other companies of comparable size and complexity. The Chairman's fee is currently £80,000 per annum. The base fee for NEDs is currently £40,000 per annum. Additional fees per annum are set out below: • SID – £10,000 • Chairman of Audit Committee – £6,000 • Chairman of Remuneration Committee – £4,000. NEDs are entitled to additional payment in the event the time requirement is above normal levels. The Chairman receives an amount of £1,750 for each additional day. NEDs receive £1,500 for each additional day.	None

Service contracts – Executive Directors

Brendan Mooney, Richard McCann and Paul Gannon all entered into new contracts with the Company effective at the time of IPO. At 1 April 2017 Mr Paul Gannon, SVP Sales, changed role to become SVP Business Development. His activities now focus on identifying longer term business opportunities for the Group, primarily in Europe and the United States. As a consequence, Mr Gannon has relocated his place of employment to Dublin, Republic of Ireland and his remuneration from 1 April 2017 will be in Euro as opposed to Pounds Sterling. Mr Gannon has subsequently signed a new contract, effective from 1 April 2017.

The key terms of all their contracts are summarised in the table below:

Provisions	Summary
Term and notice	Indefinite with 12 months' notice from either party.
Payment	Salary and discretionary annual bonus.
Benefits and other entitlements	Company pension contribution or payment in lieu of pension, car allowance, private medical insurance and permanent health insurance.
Termination	Terminable on 12 months' written notice served by either party. The Company will have a contractual right to pay the Executive Directors in lieu of all of their notice period and also to place them on garden leave during all or part of their notice period. In the event of gross misconduct, their employment will be terminable with immediate effect without the requirement for notice or payment in lieu thereof.

Letters of appointment – NEDs

The NEDs entered into letters of appointment with the Company on 1 June 2015 which are terminable in certain circumstances, including the giving of three months' written notice by either party or failure to be re-elected by shareholders.

Remuneration policy for new directors

In the event that a new Executive Director is appointed or a new service contract is entered into, the service contract would be subject to a notice period of not greater than 12 months with the director entitled to receive salary, bonus and benefits as well as participate in the current share plans. The remuneration package for the new director would be set in accordance with the terms of the approved Kainos remuneration policy in force at the time of appointment, while at the same time reflecting the experience and skill of the individual.

The new director's total remuneration would be consistent with comparative packages as advised by the Remuneration Committee's remuneration advisers. In the year of joining, the annual bonus and associated performance measures will be varied to reflect the part year. In addition, when recruiting new Executive Directors, the Remuneration Committee may need to offer additional cash and/or share-based elements on a one-time basis when it considers these to be in the best interests of Kainos and its shareholders. Such payments would be limited to the remuneration lost when leaving the former employer to take up a position with Kainos and would broadly reflect the delivery mechanism (e.g. cash, shares, options), time horizons and whether performance requirements are attached to that remuneration. Shareholders will be informed of such payments at the time of appointment. In the case of an internal appointment, any variable pay element awarded in respect of the prior role would be allowed to pay out according to its terms, adjusted as relevant to take into account the appointment. In addition, other ongoing remuneration obligations existing prior to appointment would continue as appropriate, provided that they are put to shareholders for approval at the earliest opportunity. For external and internal appointments, the Remuneration Committee may agree that Kainos will meet reasonable relocation expenses in line with market practice.

The appointment of NEDs shall be on terms substantially similar to those of the existing NEDs and in accordance with the remuneration policy for NEDs applicable at the time.

Payments for loss of office
In the event of termination, the directors will receive payments for loss of office in accordance with the termination provisions of their service contracts and letters of appointment as applicable.

The default position is that on loss of office, an Executive Director forfeits any right to any bonus payment which would otherwise have accrued in respect of that year. If an Executive is deemed a good leaver, the Executive Director will be entitled to receive a bonus pro-rated to the proportion of the year that the Executive worked.

The treatment for share-based incentives previously granted to an Executive Director will be determined based on the relevant plan rules. The default treatment will be for outstanding unvested awards to lapse on cessation of employment. In relation to awards granted under the PSP, SIP or SAYE plans, in certain prescribed circumstances 'good leaver' status may be applied and the awards may vest in full.

In respect of performance shares, awards of good leavers will normally vest subject to the achievement of any performance conditions, on the normal vesting date reduced on a pro-rata basis to reflect the portion of the vesting period elapsed at the point of departure. Under the rules of the plan, the Remuneration Committee may determine that awards vest at the point of departure to the extent that performance conditions have been met at that point (as determined by the Remuneration Committee acting reasonably) and on a reduced basis pro-rated for time unless the Remuneration Committee determines to allow vesting to a greater extent.

Employees
Kainos expects the total remuneration for employees to be at a level appropriate to attract, recruit, motivate and retain the most suitable individuals. Some employees receive a bonus, which in many cases will be a percentage of salary with an element determined by personal performance and an element determined by the Group's financial performance. For more senior employees, a higher proportion of remuneration is payable as a bonus. The benefits available are dependent on market practice in each country. The pension scheme available to an employee varies according to location with contributions at a competitive level for each country.

It is the policy of the Group to offer participation in share incentive plans to all employees. More senior employees may receive discretionary share option awards. Other employees participate in all employee arrangements.

There is no formal mechanism through which Kainos consults with employees when determining Executive Directors' remuneration but the Remuneration Committee takes into consideration the pay and benefits of employees when reviewing the remuneration of the Executive Directors.

Shareholders and statement of voting at AGM
The 2017 AGM will be the Group's second as a listed company. At the 2016 AGM, the Directors' Remuneration Policy, and the Annual Report on Remuneration, were unanimously approved on a show of hands. Kainos is keen to ensure that its shareholders are supportive of the Group's remuneration philosophy and policy. The Remuneration Committee is keen to hear shareholder feedback, with the Chairman of the Remuneration Committee as the initial point of contact, and will consider any feedback provided in advance of the forthcoming AGM and throughout the year.

Flexibility, discretion and judgement

The Remuneration Committee has attempted to ensure this policy has sufficient flexibility to deal with unusual situations and scenarios which may arise. As outlined in the policy table, the Remuneration Committee retains flexibility to determine the objectives, weightings and target levels of performance under its annual bonus at the start of each year. The Remuneration Committee may also alter the performance criteria during the year reflecting the overall circumstances and the Group's performance to ensure targets remain both challenging and appropriate.

Similarly, the Remuneration Committee retains flexibility to determine the conditions, weightings and target levels of performance share awards at the point awards are made. In addition, where performance conditions have been set, if events subsequently happen which cause the Remuneration Committee to consider that any performance condition no longer represents a fair measure of performance, the Remuneration Committee may amend the performance condition so as to be more appropriate. The alternative performance condition will be equally challenging.

External appointments

Executive Directors may accept appointments as NEDs in other companies provided that such appointments do not conflict with their duties or time commitments to the Group and subject to receiving prior written approval from the Board. They are entitled to receive the fees themselves from such appointments.

Annual Report on Remuneration

Membership, meetings and evaluation

From the date of Listing in July 2015, the Remuneration Committee comprised Tom Burnet as Chairman of the Committee, John Lillywhite and Chris Cowan.

All members of the Remuneration Committee, with the exception of John Lillywhite, are Independent NEDs. None of the members of the Remuneration Committee has any personal financial interest (other than as shareholders, to the extent disclosed in this report), conflicts of interest arising from cross-directorships, or day-to-day involvement in running the business. The Executive Directors may attend Remuneration Committee meetings by invitation. The Company Secretary acts as secretary to the Remuneration Committee.

Responsibilities

The Remuneration Committee operates within its terms of reference, which are reviewed and updated annually and are available from the Group's website at www.kainos.com.

The Remuneration Committee is directly responsible for managing all aspects of the remuneration of Executive Directors, for giving guidance on the remuneration of other members of the senior management team and supervising the workings of all the Group's share incentive plans.

Remuneration consultants

During the year, the Remuneration Committee took independent advice from h2glenfern Remuneration Advisory (a division of h2glenfern Limited). h2glenfern operates in accordance with the principles of the Code of Conduct for the Remuneration Consultants' Group in relation to executive remuneration consulting in the United Kingdom. h2glenfern does not provide other services to Kainos. For the year under review, h2glenfern received fees of £13,000 related to its work for the Remuneration Committee on operational matters.

Remuneration details

In accordance with the Regulations, the tables below set out the remuneration for each director for the year ended 31 March 2017.

Single total figure of remuneration for each director

Name	Financial year	Salary/fees[1] (000s)	Benefits (000s)	Bonus (000s)	Total (excluding pension) (000s)	Pension[2] (000s)	Incentives vested	Total (including pension) (000s)
Executive Directors								
Brendan Mooney[5]	2017	£220	£7	£151	£378	£19	N/A	£397
	2016	£216	£7	£186	£409	£19	N/A	£428
Richard McCann	2017	£195	£6	£130	£331	£10	N/A	£341
	2016	£181	£6	£155	£342	£9	N/A	£351
Paul Gannon	2017	£195	£13	£222	£430	£29	N/A	£459
	2016[3]	€15	€5	N/A	€20	€9	N/A	€29
	2016	£176	£10	£269	£455	£21	N/A	£476
NEDs								
John Lillywhite[5]	2017	£80	N/A	N/A	N/A	N/A	N/A	£80
	2016	£74	N/A	N/A	N/A	N/A	N/A	£74
Andy Malpass[4]	2017	£56	N/A	N/A	N/A	N/A	N/A	£56
	2016	£45	N/A	N/A	N/A	N/A	N/A	£45
Chris Cowan[4]	2017	£40	N/A	N/A	N/A	N/A	N/A	£40
	2016	£33	N/A	N/A	N/A	N/A	N/A	£33
Tom Burnet[4]	2017	£44	N/A	N/A	N/A	N/A	N/A	£44
	2016	£37	N/A	N/A	N/A	N/A	N/A	£37

1 Amounts noted are the total actual salary/fee payments made during FY 2017, not base salary.

2 Pension amounts for Brendan Mooney and Richard McCann are payments in lieu of pension.

3 In FY 2016 year Paul Gannon was remunerated in Euro for Republic of Ireland company services and Pounds Sterling for UK company services. From 1 June 2015 to 31 March 2017 he was paid in Pounds Sterling. From 1 April 2017 he will be paid his entire salary in Euro, as a consequence of his change in role to SVP Business Development, and relocation to Dublin, Republic of Ireland.
At the exchange rate of £1 = €1.1729 on 1 April 2017, the total remuneration is 2.2% higher than FY 2017 (including base salary, annual on-target bonus, car allowance and employer pension contribution).

4 The above independent Non-Executive Directors joined the Board on 1 June 2015. There have been no changes to their remuneration.

5 There have been no changes to the remuneration for John Lillywhite and Brendan Mooney since the IPO in July 2015.

Kainos did not make any payments to past or current directors for loss of office.

Annual bonus

The Executive Directors' bonus for the year ended 31 March 2017 was based on the revenue, adjusted pre-tax profit and sales order value targets. The structure of the bonus and targets is set out in the table below:

Objective	Weighting	Target performance (£000s)	Threshold performance (£000s)	Outcome (£000s)	Bonus payout (£000s)	Bonus payout (£000s)	Bonus payout (£000s)
					B Mooney	R McCann	P Gannon
Revenue	30%	87,107	74,032	83,504	43	37	63
Adjusted pre-tax profit	40%	14,139	11,310	14,269	73	63	107
Sales order value	30%	115,000	68,989	89,505	35	30	52
Totals	100%				151	130	222

Annual bonus payments are subject to thresholds and accelerators as set out below.

- Revenue:
  - Achievement below threshold pays zero;
  - Bonus payout on achievement between threshold and target is in 'steps', progressing to 100% bonus payout on achievement of target;
  - Achievement in excess of target pays out 100% bonus, plus 2% bonus for every 1% of achievement over the target.
- Adjusted pre-tax profit:
  - Achievement below threshold pays zero;
  - Bonus payout on achievement between threshold and target is in 'steps', progressing to 100% bonus payout on achievement of target;
  - Achievement in excess of target pays out 100% bonus, plus 1.5% bonus for every 1% of achievement over the target.
- Sales order value:
  - Achievement below threshold pays zero;
  - Bonus payout on achievement between threshold and target is in 'steps', progressing to 100% bonus payout on achievement of target;
  - Bonus payout on achievement between target and 120% pays out bonus on a straight line basis;
  - Achievement in excess of 120% of target pays out 120% of bonus, plus 1.4% bonus for every 1% of achievement over 120%.

The bonuses paid to Brendan Mooney, Richard McCann and Paul Gannon were 69%, 67% and 114% of salary respectively.

Under the remuneration policy the maximum annual bonus opportunity as a percentage of the Executive's salary is 150% for the CEO, 150% for the CFO and 225% for the SVP Business Development.

Directors' shareholdings

The interests of the directors and their connected persons in Kainos ordinary shares at 31 March were:

Name	**2017**	2016
Brendan Mooney	**14,107,020**	14,107,020
Richard McCann	**6,140,000**	6,140,000
Paul Gannon	**9,131,240**	9,131,240
John Lillywhite	**500,000**	500,000
Andy Malpass	**38,590**	38,590
Chris Cowan	**31,582**	31,582
Tom Burnet	**14,388**	14,388

Share ownership guideline

In view of the size of each of the shareholdings of the Executive Directors, the value of which is a significant multiple of their salary, the Remuneration Committee has not implemented a guideline in respect of the value of shareholding which executives should hold. There is no shareholding guideline for the NEDs.

LTIP

The Remuneration Committee granted performance and service related share awards to the Executive Directors under the PSP in 2015 and 2016 as outlined below:

Name	Date of grant	No. of ordinary shares under option	Value of award at date of grant	Exercise price per ordinary share	First exercise date	Lapsing date
Brendan Mooney	July 2015	197,842	£270,000	Nominal	July 2018	July 2025
	June 2016	56,410	£88,000	Nominal	June 2019	June 2026
Richard McCann	July 2015	136,691	£190,000	Nominal	July 2018	July 2025
	June 2016	62,500	£97,500	Nominal	June 2019	June 2026
Paul Gannon	July 2015	136,691	£190,000	Nominal	July 2018	July 2025
	June 2016	50,000	£78,000	Nominal	June 2019	June 2026

The 2015 PSP awards are subject to the following performance conditions. The vesting of 50% of the award is subject to a condition that measures growth in earnings per share (EPS) over a three year performance period up to the year ending 31 March 2018 using the financial year ended 31 March 2015 as the base year. The vesting of 50% of the award is subject to a condition that measures the Group's total shareholder return (TSR) over a three year period from the date of IPO and using the IPO price of 139p as the base value per share. Between threshold and maximum vesting, awards vest on a straight line basis.

The 2016 PSP awards are subject to the following performance conditions. The vesting of 50% of the award is subject to a condition that measures growth in earnings per share over a three year performance period up to the year ending 31 March 2019 using the financial year ended 31 March 2016 as the base year. The vesting of 50% of the award is subject to a condition that measures the Group's total shareholder return over a three year period from the date of IPO and using the price of 162p as the base value per share. Between threshold and maximum vesting, awards vest on a straight line basis.

Performance condition	EPS growth	TSR growth
Portion of award subject to this condition	50%	50%
Threshold vesting – vesting at 30% of total	9% compound growth per annum	9% compound growth per annum
Maximum vesting – 100% of total	16% compound growth per annum	16% compound growth per annum

SIP and SAYE schemes

The Executive Directors were entitled to participate in the SIP and SAYE schemes without performance conditions, on no more favourable terms than other employees with similar length of service. The SIP shares and SAYE options for the Executive Directors are shown below.

Name	2015 SIP shares	2015 SAYE options	2016 SIP shares
Brendan Mooney	2,589	–	632
Richard McCann	1,438	3,237	632
Paul Gannon	2,589	3,237	632

Directors' and Corporate Governance Report continued

Performance graphs and comparator tables

The regulations require the presentation of a number of graphs and tables setting out a comparison of company performance and CEO remuneration for the same period of time. The Board believes that the techMARK All-Share Index, of which the Group is a constituent, provides the best benchmark for comparison. The Group's share price performance against FTSE techMARK All-Share Index performance from the date of IPO in July 2015 to the end of the 2017 financial year is shown below. The Group's share price and the techMARK All-Share Index are both set to 100 at the start of the period.

Kainos share price performance against FTSE techMARK All-Share Index

CEO remuneration

The table below sets out the total remuneration delivered to the CEO over the last two years valued using the methodology applied to the single total figure of remuneration. The Remuneration Committee does not believe that the remuneration payable in its earlier years as a private company bears any comparative value to that paid in its later years and therefore the Remuneration Committee has chosen to disclose remuneration only for the two most recent financial years. The CEO held options in Kainos Software Limited which were not subject to performance conditions. These were satisfied in full, or lapsed, on or prior to listing of Kainos Group plc.

	Salary and benefits (£000s)	Annual bonus (£000s)	Total remuneration (£000s)	Bonus as percentage of maximum	Vesting of long term incentives as % of maximum
2017	£246	£151	£397	46%	n/a
2016	£242	£186	£428	57%	100%

Change in CEO remuneration and remuneration of all UK employees

The table below highlights the percentage change in the sum of salary, benefits and bonus of the Chief Executive and all UK employees for recent years. Kainos considers the comparator group of all UK employees to be representative of Kainos as a whole and a global comparator group would not result in a material variance.

Annual change	CEO's salary	UK employees' salary	CEO's annual bonus	UK employees' annual bonus	CEO's benefits	UK employees' benefits	CEO's total	UK employees' total
2017	2.0%	6.5%	(18.8%)	(10.9%)	0.0%	0.0%	(6.2%)	6.4%
2016	7.8%	6.7%	(18.2%)	(21.7%)	0.0%	0.0%	(5.4%)	5.6%

Comparison of staff remuneration to Group KPIs

Kainos employees are vital to the growth and success of the business. As a software business with a strategy focused on organic development, its primary costs are related to its employees. The profit and corporation tax figures have been included to provide greater context to staff remuneration and the total distributions to shareholders.

	Staff remuneration (£000s)	Profit before tax (£000s)	Corporation tax (£000s)	Effective tax rate	Dividends (£000s)
2013	17,402	3,480	(203)	6%	–
2014	22,954	7,056	(1,600)	23%	(651)
2015	30,954	11,837	(2,072)	18%	(1,325)
2016	35,373	14,261	(1,834)	13%	(13,309)
2017	43,747	13,320	(2,904)	22%	(7,208)

AGM

The 2017 AGM will be the Group's second since its IPO. The Directors' Annual Report on Remuneration will be put to an advisory shareholder vote.

Directors’ and Corporate Governance Report continued

Directors’ remuneration for the year commencing 1 April 2017

Salary	The Committee will continue to monitor the remuneration of Executive Directors of other companies in the IT sector and other listed companies with similar market capitalisation to ensure that the Executive Directors remain sufficiently rewarded to promote long term success. In line with the directors’ remuneration policy, the annual salaries of the Executive Directors for the year commencing 1 April 2017 are as follows: CEO: £220,000 CFO: £195,000 SVP Business Development: €243,000
Benefits	There will be no change to the benefits for the CEO or the CFO in the year commencing 1 April 2017. However, as has been mentioned, Paul Gannon will be paid in Euro from 1 April 2017.
Pension	There will be no change to the pension arrangements of the Executive Directors in the year commencing 1 April 2017.
Annual bonus	Annual bonus for the year commencing 1 April 2017 will be operated within the policy disclosed in this report. The principles of bonus criteria which will be applied to each Executive Director during the year ending 31 March 2018 will be similar to those applied during the year ended 31 March 2017. The targets for the annual bonus for 2017/18 are not being disclosed in this report as that information is deemed commercially sensitive and may be interpreted to be a forecast. That information will be disclosed in the 2018 Annual Report.
Long term incentives	The Committee intends to make further performance share awards in mid-2017. These will be made in line with the Remuneration Policy. The Committee will determine the levels, performance conditions, weighting and growth targets to be applied at the time of award and disclose them in the 2018 Annual Report.
NED remuneration	For the year commencing 1 April 2017, it is proposed that NED fees remain the same as in the year ended 31 March 2017.

On behalf of the Board

Tom Burnet
Chairman of the Remuneration Committee
26 May 2017

Audit Committee Report

As Chairman of the Audit Committee, I am pleased to introduce the Audit Committee Report for the year ended 31 March 2017. The Audit Committee has met two times during the year in May 2016 and November 2016. The Audit Committee plays a central role in the review of Kainos Group's financial reporting, risk review and internal control processes. The Committee has focused on the integrity, completeness and clarity of financial reporting, the areas where judgements and estimates are required in the financial statements and the quality and effectiveness of audit processes to complement the other risk management activities. There has been no significant change to these areas of focus during the year and the Committee will continue to monitor them.

Andy Malpass
Chairman of the Audit Committee

Composition and evaluation

In accordance with the provisions of the Code, the Audit Committee is made up of three NEDs, of which two are independent. The Audit Committee is chaired by Andy Malpass and the other members are Chris Cowan and John Lillywhite. The Board considers that Andy Malpass, who is a fellow of the Chartered Institute of Management Accountants with significant financial experience including serving as Finance Director of Fidessa group plc until October 2015, has the recent and relevant experience required to act as Chairman of the Committee. Details of relevant experience of all members of the Committee are detailed in the 'Directors' and Corporate Governance Report'.

The performance of the Committee was evaluated as part of the Board evaluation process and the conclusion was that the Committee was functioning effectively.

Responsibilities

The Committee operates within its terms of reference, which are reviewed and updated annually and are available from the Group's website at www.kainos.com. The Committee's main responsibilities include:

- monitoring the integrity of the financial statements, including the Group's annual and interim reports, announcements of preliminary results and any other formal announcement relating to its financial performance;
- advising the Board that the Annual Report is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's position and performance, business model and strategy;
- monitoring the appropriateness of accounting policies and practices along with consistent treatment year to year;
- monitoring and reviewing the adequacy and effectiveness of the Group's internal financial controls and internal control and risk management systems; and
- making recommendations to the Board on the appointment and remuneration of the external auditor, review and monitor the external auditor's performance, expertise, independence and objectivity along with the effectiveness of the audit process and its scope.

External audit

The Audit Committee advises the Board on the appointment, reappointment or removal of the Group's external auditor. Deloitte LLP is the Group's current auditor and was originally appointed in 2011. In line with EU legislation, all EU public interest entities must tender their audit every ten years. The Committee is satisfied with the effectiveness of the audit. During the year the Audit Committee reviewed and approved the scope and timetable for the interim review and final audit.

Appointment, independence and objectivity

During the year the external auditor provided no non-audit services. The Group has engaged another independent accounting firm to perform tax consulting work and other assignments to further ensure the independence and objectivity of the auditor is not compromised. The Committee received a written confirmation from the external auditor that it considered itself to be independent.

Audit partners for listed companies are ordinarily rotated every five years. However, where the audit engagement partner has already served for four or more years when a company becomes listed, that individual may continue to serve as the audit engagement partner for not more than two years after the listing of the company. Therefore, the current partner, David Crawford, must be replaced as audit partner going forward, and a new audit partner, Richard Howard, has been arranged to take over for the financial year 2018.

Assessment of effectiveness of external audit

The Committee assessed the effectiveness of the external audit process at its meeting in May 2017. The audit was substantive in approach and included significant testing in areas identified as key risks such as revenue. This gave the Committee confidence as to the overall quality of the audit. The Committee also asked Deloitte LLP to report on control findings arising from the audit as part of the year end process. In addition, feedback on the audit was obtained from management and the finance team.

Following its review of the effectiveness of the external audit and independence of the external auditor, the Committee is satisfied that independence has been maintained and that it is appropriate to reappoint Deloitte as the external auditor. The Committee therefore recommended to the Board that Deloitte be reappointed as the external auditor for 2018 and a resolution for its appointment will be submitted to the AGM.

Internal control and risk management

The Board is ultimately responsible for the overall system of internal control and risk management for the Group and for reviewing their effectiveness. The system of internal controls is designed to manage, rather than eliminate, the risks to which the Group is exposed, including the risk of failure to achieve business objectives and can provide only reasonable and not absolute assurance against material misstatement or loss. The concept of reasonable assurance recognises that the cost of control procedures should not exceed the expected benefits. Details of the principal risks are set out in the Strategic Report.

The Board confirms that Kainos has established systems, procedures and controls designed to establish an ongoing process for identifying, evaluating and managing the principal risks faced by Kainos and that they have been in place for the period under review and up to the date of approval of the Annual Report. The effectiveness of those systems, procedures and controls are regularly reviewed by the Board.

As required by the Code, the Committee has reviewed the internal controls and risk management systems, including those relating to financial reporting, information technology, business continuity, management of employees, operational and compliance matters and the Committee has confirmed to the Board that it is satisfied that Kainos has established internal controls and risk management systems that are effective and compliant with the current governance provisions.

The key elements of the Group's ongoing processes for the provision of effective internal control and risk management systems include:

- regular Board meetings to consider matters reserved for the directors' attention;
- regular management meetings held to monitor divisional performance. Management is responsible for the identification and evaluation of significant risks applicable to their area of business, together with the design and operation of suitable internal controls;
- maintenance of a corporate risk register to identify the risks facing the business. The key risks are summarised for review by the Audit Committee;
- documentation of key policies and procedures; and
- preparation of a comprehensive annual budgetary process for review and approval by the Board. An updated forecast regularly prepared throughout the year. The operating results are reported monthly to the Board and compared to the latest forecast with explanations for all significant variances.

Key matters considered in relation to the financial statements

During the year ended March 2017 the Committee reviewed the results of the external audit for the previous financial year including reviewing the 2016 Annual Report and Preliminary Announcement, the external auditor's half year review and the half year results as well as the external audit plan for 2017. In May 2017, the Committee received the 2017 Annual Report including the financial statements contained within it, the Preliminary Results Announcement for the year ended March 2017 and reports from the external auditor on their audit of the financial statements and Annual Report.
The Committee's prime areas of focus were:

- the integrity, completeness and consistency of financial reporting, including the adequacy, clarity and appropriateness of disclosures. This included reviewing the Annual Report and concluding that it was fair, balanced and understandable;
- the areas where significant judgements and estimates are required in the financial statements;
- the scope and programme of external audit, along with the quality and effectiveness of external audit processes;
- the materiality level used by the external auditor, concluding that it should be consistent with the previous year;
- whether the going concern basis of accounting should continue to apply in the preparation of the annual financial statements and whether the period applied to the viability statement was appropriate;
- reviewing the processes and systems to identify and mitigate the financial and non-financial risks and to consider the appropriateness of the controls to reduce the risk of fraud and exposure to bribery and corruption; and
- the appropriateness of the 'whistleblowing' procedures in place whereby staff may confidentially raise concerns about possible improprieties.

The preparation of financial statements requires management to make assumptions, judgements and estimates and the material ones are detailed in note 4 of the consolidated financial statements. The key areas of judgements, estimates and assumptions that have been reviewed and considered by the Committee were:

- revenue recognition in relation to significant contracts and implementations and the level of contract or fixed price provisioning for rectification and irrecoverable accrued income. The Group has a clear revenue recognition policy, described in note 3, and performs regular contract reviews with relevant staff. In addition, the Committee discussed and provided input into management's proposed process for the implementation of IFRS15 "Revenue from Contracts with Customers" and requested further updates on progress and impact assessment prior to adoption. The Committee has also obtained comfort over the completeness and valuation of any contract or fixed price provisions. Relevant management are consulted with on a project by project basis to assess the level of provisioning required. The Committee is satisfied that the internal processes and controls are appropriate;
- recognition of income in relation to government grants. The Group has a clear policy, described in note 3, and the Committee is satisfied that the internal processes and controls are appropriate;
- development costs and the approach to their capitalisation. The Committee received updates from management and the external auditor and was satisfied that the methodology and process were appropriate. The Committee concurred with management that currently none of the development costs should be capitalised; and
- the tax complexity and risk related to the multinational operations of the Group and the areas of uncertainty that arise. The Committee considered the appropriateness of deferred tax assets and tax provisions held and an analysis of the RDEC rules and their impact on the reported results in relation to the updates and reports it had received and concluded that the treatment adopted was fair and reasonable.

Internal audit

The Group operates an audit programme which forms part of its ISO9001 (Quality Management System), ISO20000 (Information Technology Service Management System) and ISO27001 (Information Security Management System) certifications. As part of the certification process Kainos undergoes a bi-annual assessment to ensure that all of the controls are robust and any Kainos assets are appropriately protected. Information Security risks are assessed and reviewed regularly in IT steering meetings with the Group's senior management.

Directors' and Corporate Governance Report continued

Kainos also participates in additional third party assessments for public and private sector customers to ensure that associated security controls are effective and address any related risks. The key elements of the Group's internal control framework and procedures are noted above, while the principal risks faced by the Group are set out in the 'Risk Factors and Uncertainties' section of the Strategic Report. Through the various audit activities outlined above and the close control of operations exercised by the Executive Directors as well as the centralisation of financial management in Belfast the Group does not require these activities to be separated into a standalone audit function.

The Audit Committee will review the internal control framework and procedures on an ongoing basis giving consideration to whether certain areas should be looked at more closely. In doing so, the Audit Committee will continue to monitor whether there is a requirement for a dedicated internal audit function.

Nominations Committee Report

Membership, meetings and evaluation

The Nominations Committee, which is chaired by John Lillywhite, comprises John Lillywhite, Chris Cowan and Tom Burnet and is therefore compliant with the requirements of the Code.

The performance of the Committee was evaluated as part of the Board evaluation process during the year and the conclusion was that the Committee was functioning effectively.

Responsibilities

The Committee operates within its terms of reference, which are reviewed and updated annually and are available from the Group's website at www.kainos.com. The Committee's main responsibilities are to advise and make recommendations to the Board on the following matters:

- the size, structure and composition of the Board;
- succession planning of Board members; and
- the appointment of new directors and the re-appointment of existing directors.

Matters considered during the year

During the year ended 31 March 2017, a formal Board evaluation was undertaken in line with the recommendation of the Code, this being coordinated by the Chairman and Company Secretary. The outcome of the review, completed in January 2017, was largely positive and constructive. The Committee recognises the importance of succession planning and the role it plays in maintaining a continuous level of quality in management and reducing the level of instability that may arise following unforeseen events, such as the departure of a key individual. The Nominations Committee, in conjunction with the Board, formally discussed succession planning at each of the three meetings held during the year, with extensive progress made in this area. This is a key area that the Committee will continue to monitor on an ongoing basis.

Other statutory disclosures

In accordance with Section 414C (11) of the Companies Act 2006, to the extent they are not addressed in the Directors' and Corporate Governance Report, the disclosures relating to the following matters are included in the Strategic Report: environmental matters (including greenhouse gas emissions and the impact of the Group's business on the environment); the Group's employees (including equal opportunities, gender diversity and employee engagement); and, social, community and human rights issues (including corporate social responsibility).

The financial results and position are shown in the financial statements. A fuller explanation of the results, including the recommended dividend and financial position, is provided in the Overview and the Finance Review sections of the Strategic Report and the notes to the financial statements.

No political donations were made during the year ended 31 March 2017.

There are no off-balance sheet arrangements. Details of the trusts relating to Kainos' share incentive plans are set out in note 21 to the consolidated financial statements. The shares held by the trust rank pari passu with all the other shares in issue and have no special rights.

For the purposes of LR9.8.4C R, the information required to be disclosed by LR9.8.4 R can be found in the following locations:

Section	Topic	Location
1	Interest capitalised	Not applicable
2	Publication of unaudited financial information	Not applicable
4	Details of long term incentive schemes	Not applicable
5	Waiver of emoluments by a director	Not applicable
6	Waiver of future emoluments by a director	Not applicable
7	Non pre-emptive issues of equity for cash	Not applicable
8	Section (7) in relation to major subsidiary undertakings	Not applicable
9	Parent participation in a placing by a listed subsidiary	Not applicable
10	Contracts of significance	Directors' report
11	Provision of services by a controlling shareholder	Not applicable
12	Shareholder waivers of dividends	Not applicable
13	Shareholder waivers of future dividends	Not applicable
14	Agreements with controlling shareholders	Not applicable

Share capital and articles of association
Details of the called-up and fully paid share capital are set out in note 19 to the consolidated financial statements. The rights and obligations attaching to the shares and the powers of the directors are set out in the Articles of Association, copies of which can be obtained from Companies House. There are no restrictions on the voting rights attached to the shares and no person holds securities carrying special rights with regard to control.

Authority to purchase own shares
Kainos holds a general authority to purchase up to 11,831,853 of ordinary shares in the market. This represented approximately 10% of the Kainos' issued share capital as at 21 July 2016, as voted on and approved by shareholders at the 2016 AGM. No purchase of shares has been made pursuant to this authority. There is no present intention to use such authority, but the Board considers it desirable that the possibility of making such purchases under appropriate circumstances remains available. A similar authority will be requested at the forthcoming AGM, again limited to a maximum of 10% of the issued share capital. The Board intends only to exercise this authority if it believes that it will lead to an increase in earnings per share for the remaining shareholders.

The appointment and replacement of directors is governed by the Articles of Association and the Nominations Committee's Terms of Reference. The Articles of Association may be amended by a special resolution.

Disclosure of information to auditor
The directors who held office at the date of approval of this Directors' and Corporate Governance Report confirm that, so far as they are each aware, there is no relevant audit information of which the auditor is unaware and each director has taken the steps that he or she ought to have taken as a director to ascertain any relevant audit information and to establish that the auditor is aware of that information.

Significant agreements – change of control
Members of the Group are subject to certain customer contracts which require them to notify the relevant counterparty of a change of control of the Group which, in some instances, may allow the relevant counterparty to terminate their contracts with the Group. The Directors are not aware and do not anticipate any reason or circumstances where any such customers would wish to trigger their termination rights under such change of control provisions. The only significant agreements with change of control provisions are the share incentive plans. Under the CSOP, SAYE and Polish share plans, on a change of control, options and awards that are not lapsed would generally vest in full. The PSP awards would also vest subject to the satisfaction of any performance conditions at the time, but these would be time pro-rated. Other than as set out in this statement, Kainos is not party to any other significant agreements that take effect, alter or terminate upon a change of control following a takeover or upon a takeover bid.

Directors' and Corporate Governance Report continued

Compliance with the UK Corporate Governance Code

Kainos is committed to high standards of corporate governance and is subject to the principles of the UK Corporate Governance Code. In respect of the year ended 31 March 2017 Kainos has complied with all of the provisions of the Code with the exception of two areas mentioned above (relating to the absence of an internal audit function and the non-independence of the NED/Chairman, John Lillywhite).

Dialogue with shareholders

Kainos values the views of its shareholders and recognises their interests in its strategy and performance. The CEO and CFO hold briefing meetings with analysts and institutional shareholders, primarily following the announcement of interim and preliminary results but also at other times during the year as may be suitable.

The CEO and CFO provide feedback to the Board from meetings with shareholders. The Board also obtains formal feedback from analysts and institutional shareholders via Kainos' PR adviser and financial advisers. Communication with private investors is through the Annual Report and the AGM. Financial and other information is made available on the website, www.kainos.com, which is regularly updated.

Principal shareholders

The following have disclosed that they have an interest in 5% or more of the issued ordinary share capital. At 24 May 2017, the last holding notified to the Company is shown below.

Investor	Ordinary 0.5p shares	% of issued share capital
Qubis	18,947,257	16.0%
Brendan Mooney	14,107,020	11.9%
Paul Gannon	9,131,240	7.7%
Mawer Investment Management Limited	7,747,955	6.6%
Standard Life Investments	7,132,831	6.0%
Brian Gannon	6,217,440	5.3%
Richard McCann	6,140,000	5.2%

Going concern and long term viability

Kainos' business activities and position in its market are described in the Overview, Business Model and Strategy, and Risks sections of the Strategic Report. The financial position, cash flows and liquidity position are described in the Finance Review and the notes to the financial statements. In addition, the notes to the financial statements include Kainos' objectives, policies and processes for managing its capital, its financial risk management objectives and its exposures to credit and liquidity risk.

Having reviewed the future plans and projections for the business and its current financial position, the Board believes that Kainos is well-placed to manage its business risks successfully. Kainos has adequate financial resources, no borrowings, a good level of recurring revenue, and a broad spread of customers. As a consequence of these factors and having reviewed the forecasts for the coming year, the Board has a reasonable expectation that Kainos has adequate resources to continue in operational existence for the foreseeable future, a period of not less than 12 months from the date of this report. For this reason, it continues to adopt the going concern basis of accounting in preparing the annual financial statements.

In addition to the going concern consideration, the directors have assessed the Group's viability over a longer period than 12 months. The assessment was conducted over a three year period, ending March 2020. A period of three years was selected for the following reasons:

- the Group's strategic plan encompasses a period of three years;
- the period identified is underpinned by financial budgets and forecasts; and
- this duration is considered an adequate period to assess the rate of change in each of the key divisions.

In performing the assessment, the Group's long term strategy and focus, the growing demand for its products and services, the increasing level of recurring revenue and low customer attrition, the track record of strong cash generation and a healthy cash balance with no debt from financial institutions were all taken into consideration. Consideration has also been given to the risks of regional and political changes in the Group's main markets. The Board believes that the Kainos global structure of its entities means that it is less susceptible to the effects of regional changes, as the vast majority of the Group's costs are incurred in sterling with most revenue also being earned in Sterling and revenues earned in foreign currency including Euro and US Dollar have most of their costs in foreign currency and the weakened Pound has also lead to increased Sterling amount on translation. From a political perspective, despite uncertainty in the UK, the US and mainland Europe over the past year, the Group remains optimistic that its portfolio of digital services and platforms continues to be in demand, and that it remains well-positioned to help public and private sector organisations in their digital transformation initiatives.

The review included sensitivity analysis on the future performance and solvency over three years and also for the principal risks facing the business in severe but reasonable scenarios. Based on the results of this assessment, the directors have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over a three year period of their assessment. In doing so it is recognised that such future assessments are subject to a level of uncertainty that increases with time and, therefore, future outcomes cannot be guaranteed or predicted with certainty.

Directors' responsibilities statement in respect of the Annual Report and the financial statements
The directors are responsible for preparing the Annual Report and the Group and Company financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare Group and Company financial statements for each financial year. Under that law they are required to prepare the Group financial statements in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU and Article 4 of the IAS Regulation and have also chosen to prepare the parent company financial statements in accordance with Financial Reporting Standard 101 Reduced Disclosure Framework.

Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and Company and of their profit or loss for that period.

In preparing the parent company financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether Financial Reporting Standard 101 Reduced Disclosure Framework has been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

In preparing the Group financial statements, the directors are required to:

- properly select and apply accounting policies;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- provide additional disclosures when compliance with the specific requirements in IFRSs are insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance; and
- state whether they have been prepared in accordance with IFRSs as adopted by the EU; and
- make an assessment of the Company's ability to continue as a going concern.

Directors' and Corporate Governance Report continued

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain transactions and disclose with reasonable accuracy at any time the financial position and enable them to ensure that the financial statements comply with the Companies Act 2006. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets and to prevent and detect fraud and other irregularities.

Under applicable law and regulations, the directors are also responsible for preparing a Strategic Report, Directors' Report, Directors' Remuneration Report and Corporate Governance Statement that comply with that law and those regulations.

The directors are responsible for the maintenance and integrity of the corporate and financial information included on Kainos' website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

The directors confirm that to the best of their knowledge:

- the financial statements, prepared in accordance with IFRSs as adopted by the EU and applicable law, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the undertakings included in the consolidation taken as a whole;
- the Directors' and Corporate Governance Report includes a fair review of the development and performance of the business and the position of the Company and its subsidiaries included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face; and
- the Annual Report, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's position, performance, business model and strategy.

On behalf of the Board

John Lillywhite
Chairman
26 May 2017

Independent Auditor's Report to the members of Kainos Group plc

Opinion on financial statements of Kainos Group plc

In our opinion:

- the financial statements give a true and fair view of the state of the Group's and of the parent company's affairs as at 31 March 2017 and of the Group's profit for the year then ended;
- the Group financial statements have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union;
- the parent company financial statements have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice, including FRS 101 "Reduced Disclosure Framework"; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

The financial statements that we have audited comprise:

- the Consolidated Statement of Comprehensive Income;
- the Consolidated and Parent Company Statements of Financial Position;
- the Consolidated Cash Flow Statement;
- the Consolidated and Parent Company Statements of Changes in Equity; and
- the related Consolidated notes 1 to 25 and the Parent Company notes 1 to 9.

The financial reporting framework that has been applied in the preparation of the Group financial statements is applicable law and IFRSs as adopted by the European Union. The financial reporting framework that has been applied in the preparation of the parent company financial statements is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice), including FRS 101 "Reduced Disclosure Framework".

Summary of our audit approach

Key risks	The key risks that we identified in the current year were: • Revenue recognition • Contract provisioning • Recognition of Research and Development Credits (RDEC) Within this report, any new risks are identified with and any risks which are the same as the prior year identified with .
Materiality	The materiality that we used in the current year was £663,000 which was determined on the basis of 5% of operating profit before exceptional items.
Scoping	Consistent with last year, we focused our Group audit scope primarily on the audit work at the Belfast location, where all entities in this location are subject to a full audit. The remaining five entities were subject to an audit of specified account balances.
Significant changes in our approach	A new key risk has been identified relating to the recognition of research and development credits (RDEC), which are recognised above the operating profit line where in prior years' research and development tax credits were recognised as a deduction against the tax charge.

Independent Auditor's Report to the members of Kainos Group plc continued

Going concern and the directors' assessment of the principal risks that would threaten the solvency or liquidity of the Group

As required by the Listing Rules we have reviewed the directors' statement regarding the appropriateness of the going concern basis of accounting contained within note 3 to the financial statements and the directors' statement on the longer term viability of the Group contained within the Directors' and Corporate Governance Report.	**We confirm that we have nothing material to add or draw attention to in respect of these matters.**
We are required to state whether we have anything material to add or draw attention to in relation to: • the directors' confirmation in the Audit Committee Report that they have carried out a robust assessment of the principal risks facing the Group, including those that would threaten its business model, future performance, solvency or liquidity; • the disclosures in the Strategic Report that describe those risks and explain how they are being managed or mitigated; • the directors' statement in note 3 to the financial statements about whether they considered it appropriate to adopt the going concern basis of accounting in preparing them and their identification of any material uncertainties to the Group's ability to continue to do so over a period of at least 12 months from the date of approval of the financial statements; and • the directors' explanation in the Directors' and Corporate Governance Report as to how they have assessed the prospects of the Group, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.	**We agreed with the directors' adoption of the going concern basis of accounting and we did not identify any such material uncertainties. However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the Group's ability to continue as a going concern.**

Independence

We are required to comply with the Financial Reporting Council's Ethical Standards for Auditors and confirm that we are independent of the Group and we have fulfilled our other ethical responsibilities in accordance with those standards.	**We confirm that we are independent of the Group and we have fulfilled our other ethical responsibilities in accordance with those standards. We also confirm we have not provided any of the prohibited non-audit services referred to in those standards.**

Our assessment of risks of material misstatement

The assessed risks of material misstatement described below are those that had the greatest effect on our audit strategy, the allocation of resources in the audit and directing the efforts of the engagement team.

A prior year key risk relating to Deconsolidation Adjustments has been removed. As a result of the implementation of a new accounting system for the year ended 31 March 2017 this eliminated the need for the deconsolidation process and the associated risk.

Revenue recognition	
Risk description	Revenue consists of revenues arising from consulting services, licence revenue, and support and maintenance contracts. We have identified that there was a risk that the correct revenue recognition policy may not have been applied to contracts primarily due to the following factors: • multi-element contracts may not have been correctly unbundled where they contain licence, time and materials and support elements; • inaccurate cost to complete estimates may have been used for fixed price contracts accounted for under a percentage of completion basis; and • incorrect cut-off may have occurred for public sector contracts who wished to spend available budgets before 31 March public sector year end. Revenue recognition has been identified in the Audit Committee Report as a signficiant financial reporting item. Management's accounting policies for revenue are detailed within note 3 to the financial statements, with the critical judgements applied in revenue recognition set out in note 4 to the financial statements.
How the scope of our audit responded to the risk	In order to address the risk, we: • assessed the design and implementation of the controls relating to revenue recognition; • carried out a review of the appropriateness of revenue recognition policies adopted under IFRS including disclosures in the financial statements; • selected a sample of contracts, including public sector contracts signed towards the end of the year and contracts for new products/services. Our sample selection involved identifying contracts with certain characteristics which were determined to be of audit interest. We performed detailed testing on these including performing a recalculation of revenue to be recognised based on the contract terms and comparing this to actual revenue, with each contractual element reviewed to assess whether the contract had been correctly unbundled by the Group for recognition purposes; • performed detailed testing of work in progress and advance billing including verifying the figure is appropriate based on the contracts, revenue recognised and invoices issued in the year; and • performed testing on the progress against budget and delivery milestones of fixed price contracts selected for testing to assess whether the revenues recognised to date were appropriate; this work included reviewing the post year end progress which had been achieved, and meeting directly with the project managers.
Key observations	We concluded that the revenue recognition policy has been applied appropriately.

Independent Auditor's Report to the members of Kainos Group plc continued

Contract provisioning	
Risk description	Kainos is engaged in contracts with customers where the fees are fixed and also where the technical complexity of the project is high. A risk exists that provisions have not been identified for either irrecoverable accrued income or for rectification costs associated with specific contracts given both the value of accrued income, the existence of fixed price contractsand the scale of individual projects. The level of contract provisioning for rectification and irrecoverable accrued income has been identified in the Audit Committee Report as a signficiant financial reporting item. Management's associated accounting policies are detailed in note 3 to the financial statements.
How the scope of our audit responded to the risk	We completed the following procedures in respect of this risk: • assessed the design and implementation of controls in place around the recording and review of accrued income and the process for identification of provisions; • reviewed the composition of the accrued income balance at year end, and challenged the ageing of accrued income balances at this date by identifying any trends which could indicate a recoverability issue; • any provisions identified by management were assessed both for completeness and valuation with the rationale for each provision challenged with management and supporting documentation obtained; • met with senior operational staff in each business unit to identify any concerns arising from projects and assess whether any potential provisions have been approved; • obtained direct confirmation from Kainos Group plc's legal department of any ongoing legal or contractual issues; and • considered the history of provisioning within the entity and examined the settlement of prior year provisions to assess the accuracy of management's prior year estimates.
Key observations	We concluded that management have appropriately applied the accounting policies in identifying any contract provisioning requirements.

Recognition of research and development credits (RDEC)	
Risk description	The financial statements of Kainos Group plc include disclosure of significant assumptions made in respect of the eligibility of research and development costs for tax relief. In the current year, Kainos Group plc has implemented the research and development expenditure credit regime (RDEC) with recognised RDEC grants for the period totalling £1.7 million. These costs were previously assessed and recognised as Research and Development tax credits in the financial statements. The 2015 and 2016 Research and development taxation claims have been resubmitted as RDEC grant claims. These had previously been submitted under the R&D tax credit deduction regime. A risk has been identified over the appropriateness of assumptions regarding the eligibility of research and development costs for RDEC grant support and the adequacy of disclosure in the financial statements of the nature and extent of these assumptions. The accuracy and disclosure of RDEC assumptions has been identified in the audit committee report on page as a signficiant financial reporting item. Management's associated accounting policies are detailed in note 3 to the financial statements, with the material judgements relating to RDEC explained in note 4 to the financial statements.
How the scope of our audit responded to the risk	To address this risk, we: • assessed management's process to calculate the qualifying research and development costs and assessed the design and implementation of the controls to address the significant risk; • completed the audit of tax with the involvement of a member of the audit team who is a tax specialist working under the supervision of a separate tax specialist audit partner and the audit partner; • obtained the Board paper on the treatment of RDEC costs and challenged against HMRC qualifying criteria the underlying assumptions on the eligibility of costs for relief contained in this document; • assessed the conclusions reached by the Board on the quantification of amounts to be included in the financial statements; • challenged the completeness and clarity of the disclosures relating to RDEC including assessing whether they are consistent with accounting standards and other commentary in the Annual Report.
Key observations	We concluded that management's assumptions regarding the recognition of RDEC income appear reasonable and that appropriate related disclosures associated with the receipt of this income have been included in the financial statements.

These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

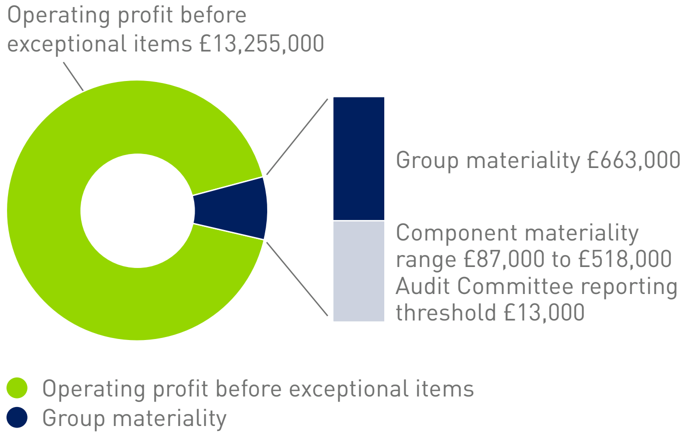
Independent Auditor's Report to the members of Kainos Group plc continued

Our application of materiality

We define materiality as the magnitude of misstatement in the financial statements that makes it probable that the economic decisions of a reasonably knowledgeable person would be changed or influenced. We use materiality both in planning the scope of our audit work and in evaluating the results of our work.

Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

Group materiality	£663,000 (2016: £677,000)
Basis for determining materiality	5% (2016: 5%) of operating profit before exceptional items (as disclosed in note 5).
Rationale for the benchmark applied	Operating profit before exceptional items has been chosen as the basis for determining materiality as we determine this to be the most relevant measure to users of the financial statements.



We agreed with the Audit Committee that we would report to the Committee all audit differences in excess of £13,000 (2016: £13,000), as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds. We also report to the Audit Committee on disclosure matters that we identified when assessing the overall presentation of the financial statements.

An overview of the scope of our audit

Our Group audit was scoped by obtaining an understanding of the Group and its environment, including Group-wide controls, and assessing the risks of material misstatement at the Group level. Based on that assessment, we focused our Group audit scope primarily on the audit work at the Belfast location, where all of the UK and Republic of Ireland entities' finance functions are managed. Consistent with last year, all of these were subject to a full audit, whilst the remaining entities, Kainos Evolve Inc., Kainos WorkSmart Inc., Kainos Worksmart GmbH and Kainos Software Poland Spólka z.o.o, were subject to an audit of specified account balances. The extent of our testing was based on our assessment of the risks of material misstatement and of the materiality of the Group's operations at those locations. Our audit work was executed at levels of materiality applicable to each individual entity which were lower than Group materiality and ranged from £87,000 to £518,000 (2016: £46,000 to £541,400).

Opinion on other matters prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:

- the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006;
- the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the Strategic Report and the Directors' Report have been prepared in accordance with applicable legal requirements.

In the light of the knowledge and understanding of the Company and its environment obtained in the course of the audit, we have not identified any material misstatements in the Strategic Report and the Directors' Report.

Matters on which we are required to report by exception

Adequacy of explanations received and accounting records Under the Companies Act 2006 we are required to report to you if, in our opinion: • we have not received all the information and explanations we require for our audit; or • adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or • the parent company financial statements are not in agreement with the accounting records and returns.	**We have nothing to report in respect of these matters.**
Directors' remuneration Under the Companies Act 2006 we are also required to report if in our opinion certain disclosures of directors' remuneration have not been made or the part of the Directors' Remuneration Report to be audited is not in agreement with the accounting records and returns.	**We have nothing to report arising from these matters.**
Corporate Governance Statement Under the Listing Rules we are also required to review part of the Corporate Governance Statement relating to the Company's compliance with certain provisions of the UK Corporate Governance Code.	**We have nothing to report arising from our review.**
Our duty to read other information in the Annual Report Under International Standards on Auditing (UK and Ireland), we are required to report to you if, in our opinion, information in the Annual Report is: • materially inconsistent with the information in the audited financial statements; or • apparently materially incorrect based on, or materially inconsistent with, our knowledge of the Group acquired in the course of performing our audit; or • otherwise misleading. In particular, we are required to consider whether we have identified any inconsistencies between our knowledge acquired during the audit and the directors' statement that they consider the Annual Report is fair, balanced and understandable and whether the Annual Report appropriately discloses those matters that we communicated to the audit committee which we consider should have been disclosed.	**We confirm that we have not identified any such inconsistencies or misleading statements.**

Independent Auditor's Report to the members of Kainos Group plc continued

Respective responsibilities of directors and auditor

As explained more fully in the Directors' Responsibilities Statement, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). We also comply with International Standard on Quality Control 1 (UK and Ireland). Our audit methodology and tools aim to ensure that our quality control procedures are effective, understood and applied. Our quality controls and systems include our dedicated professional standards review team and independent partner reviews.

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Group's and the parent company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

David Crawford.

David Crawford CA
(Senior Statutory Auditor)

for and on behalf of Deloitte LLP
Chartered Accountants and Statutory Auditor
Glasgow, United Kingdom
26 May 2017

Consolidated income statement

	Note	**2017 (£000s)**	2016 (£000s)
CONTINUING OPERATIONS			
Revenue	3, 5	**83,504**	76,594
Cost of sales	5	**(39,968)**	(39,485)
GROSS PROFIT	5	**43,536**	37,109
Operating expenses excluding share-based payments	5	**(29,332)**	(23,050)
Share-based payments	21	**(949)**	(524)
Operating expenses		**(30,281)**	(23,574)
OPERATING PROFIT BEFORE EXCEPTIONAL ITEMS		**13,255**	13,535
Exceptional gain on disposal of investment	8	**–**	1,981
Exceptional expenses in relation to IPO	8	**–**	(1,297)
Exceptional items	8	**–**	684
OPERATING PROFIT	5, 6	**13,255**	14,219
Finance income		**66**	42
Finance expense		**(1)**	–
PROFIT BEFORE TAX		**13,320**	14,261
Taxation on ordinary activities	9	**(2,904)**	(1,834)
PROFIT FOR THE YEAR		**10,416**	12,427

Consolidated statement of comprehensive income

	Note	**2017 (£000s)**	2016 (£000s)
PROFIT FOR THE YEAR		**10,416**	12,427
Other comprehensive income:			
Currency translation difference		**(249)**	–
TOTAL COMPREHENSIVE INCOME FOR THE YEAR		**10,167**	12,427
EARNINGS PER SHARE			
Basic	11	**8.9p**	10.7p
Diluted	11	**8.7p**	10.6p

Consolidated statement of financial position

	Note	2017 (£000s)	2016 (£000s)
NON-CURRENT ASSETS			
Property, plant and equipment	12	**2,002**	2,086
Investments	14	**900**	900
Other non-current assets	16	**324**	379
		3,226	3,365
CURRENT ASSETS			
Trade and other receivables	15	**18,750**	15,048
Prepayments		**1,559**	1,970
Corporation tax		**–**	1,355
Accrued income		**3,677**	5,222
Cash and bank balances		**23,722**	15,045
		47,708	38,640
TOTAL ASSETS		**50,934**	42,005
CURRENT LIABILITIES			
Trade creditors and accruals	18	**(8,683)**	(7,901)
Deferred income	18	**(6,320)**	(4,218)
Corporation tax	18	**(2,075)**	–
Other tax and social security	18	**(3,573)**	(3,637)
		(20,651)	(15,756)
NON-CURRENT LIABILITIES			
Other provisions	18	**(297)**	(297)
Deferred tax liability	17	**–**	(29)
		(297)	(326)
TOTAL LIABILITIES		**(20,948)**	(16,082)
NET ASSETS		**29,986**	25,923
EQUITY			
Share capital	19	**592**	590
Share premium account	19	**1,626**	1,607
Capital reserve	19	**667**	668
Share-based payment reserve		**1,279**	524
Translation reserve		**(249)**	–
Retained earnings	19	**26,071**	22,534
TOTAL EQUITY		**29,986**	25,923

Richard McCann
Director
26 May 2017

Consolidated statement of changes in equity

for the year ended 31 March 2017

	Share capital (£000s)	Share premium (£000s)	Capital reserve (£000s)	Share-based payment reserve (£000s)	Translation reserve (£000s)	Retained earnings (£000s)	Total equity (£000s)
BALANCE AT 31 MARCH 2015 (AUDITED)	549	521	54	–	–	22,606	23,730
BALANCE AT 31 MARCH 2015 (RESTATED)[1]	549	–	575	–	–	22,606	23,730
Profit and total comprehensive income	–	–	–	–	–	12,427	12,427
Premium on shares issued prior to reorganisation (note 19)	–	–	100	–	–	–	100
Share-based payment expense (note 21)	–	–	–	524	–	–	524
Current tax for equity-settled share-based payments	–	–	–	–	–	917	917
Deferred tax for equity-settled share-based payments	–	–	–	–	–	(107)	(107)
Issue of share capital	41	1,607	(7)	–	–	–	1,641
Dividends	–	–	–	–	–	(13,309)	(13,309)
BALANCE AT 31 MARCH 2016	590	1,607	668	524	–	22,534	25,923
Profit for the year	–	–	–	–	–	10,416	10,416
Other comprehensive income	–	–	–	–	(249)	–	(249)
Total comprehensive income for the year	–	–	–	–	(249)	10,416	10,167
Share-based payment expense (note 21)	–	–	–	949	–	–	949
Adjustments in respect of prior periods	–	–	–	(194)	–	194	–
Current tax for equity-settled share-based payments	–	–	–	–	–	(12)	(12)
Deferred tax for equity-settled share-based payments	–	–	–	–	–	147	147
Issue of share capital	2	19	(1)	–	–	–	20
Dividends	–	–	–	–	–	(7,208)	(7,208)
BALANCE AT 31 MARCH 2017	**592**	**1,626**	**667**	**1,279**	**(249)**	**26,071**	**29,986**

1 In connection with the admission to the London Stock Exchange, the Group undertook a reorganisation of its corporate structure which resulted in Kainos Group plc becoming the ultimate holding company of the Group. The transaction was accounted for as a capital reorganisation with the consolidated financial statements (including comparative information) of the Group reflecting the predecessor carrying amounts of Kainos Software Limited.

Consolidated cash flow statement

at 31 March 2017

	2017 (£000s)	2016 (£000s)
NET CASH FROM OPERATING ACTIVITIES	**16,927**	9,761
INVESTING ACTIVITIES		
Purchases of trading investments	**–**	(900)
Proceeds on disposal of investment	**–**	1,981
Purchases of property, plant and equipment	**(813)**	(1,022)
NET CASH (USED IN)/FROM INVESTING ACTIVITIES	**(813)**	59
FINANCING ACTIVITIES		
Dividends paid	**(7,208)**	(13,309)
Proceeds on issue of shares	**20**	1,741
NET CASH USED IN FINANCING ACTIVITIES	**(7,188)**	(11,568)
NET INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS	**8,926**	(1,748)
Cash and cash equivalents at beginning of year	**15,045**	16,793
Effects of foreign exchange rate changes	**(249)**	–
CASH AND CASH EQUIVALENTS AT END OF YEAR	**23,722**	15,045

Net cash from operating activities

	2017 (£000s)	2016 (£000s)
Profit for the year	**10,416**	12,427
Adjustments for:		
Income tax expense	**2,904**	1,834
Share-based payment expense	**949**	524
Gain on investment disposal	**–**	(1,981)
Government grants released	**(11)**	(11)
Depreciation	**897**	687
RDEC grant	**(1,715)**	–
Decrease in provisions	**–**	(208)
Derivative financial instruments	**–**	(98)
Operating cash flows before movements in working capital	**13,440**	13,174
Decrease/(increase) in receivables	**24**	(1,657)
Increase in payables	**3,155**	852
Cash generated by operations	**16,619**	12,369
Income taxes received/(paid)	**308**	(2,608)
NET CASH FROM OPERATING ACTIVITIES	**16,927**	9,761

Notes to the consolidated financial statements

1. General information and basis of preparation

Kainos Group plc ("the Company") is a company incorporated and domiciled in the UK (company registration number 09579188), having its registered office at 4th Floor, 111 Charterhouse Street, London EC1M 6AW.

The financial statements are presented in Pounds Sterling and rounded to the nearest thousand. The consolidated financial statements consolidate those of the Company and its subsidiaries (together "Kainos", or "the Group").

The Group's operations and principal activities are outlined in the Strategic Report. The financial position is outlined in the Finance Review and the notes to the financial statements.

The financial statements were authorised for issue by the directors on 26 May 2017.

2. Adoption of new and revised standards

At the date of authorisation of these consolidated financial statements, the following standards and amendments have been adopted for the first time, none of which had an impact on the consolidated or Company's financial statements:

- IAS16 and IAS38 Clarification of Acceptable Methods of Depreciation and Amortisation (amendments).
- IAS27 Equity Method in Separate Financial Statements (amendments).
- Annual Improvements to IFRSs 2012–2014 Cycle – various standards.
- IFRS10, IFRS12 and IAS28 Investment Entities: Applying the Consolidation (amendments).
- IAS1 Disclosure Initiative (amendments).

The accounting policies set out below have, unless otherwise stated, been applied consistently in the consolidated and Company financial statements to all periods presented.

Recent accounting developments

The following standards and interpretations which have not been applied in these consolidated financial statements were in issue but not yet mandatory and early adoption has not been applied.

- IAS7 Disclosure Initiative (amendments).
- IAS12 Recognition of Deferred Tax Assets for Unrealised Losses (amendments).
- IFRS15 Revenue from Contracts with Customers.
- IFRS9 Financial Instruments.
- IFRS16 Leases.
- IFRS2 Classification and Measurement of Share-based Payment Transactions (amendments).

With the exception of IFRS15, the directors do not expect that the adoption of the standards and interpretations listed above will have a material impact on the consolidated financial statements of the Group in future periods. IFRS15 will become effective from January 2018 and apply to an entity's first financial statements for a period beginning on or after this date which for Kainos will mean for the financial year beginning 1 April 2018. The Group is in the initial stage of planning its evaluation of the impact of the standard. IFRS15 contains a new set of principles on when to recognise and measure revenue as well as new requirements related to presentation and disclosure. Under IFRS15, revenue earned from contracts with customers will be recognised based on a five-step model which requires, for each contract, the transaction price to be apportioned to the separate performance obligations arising under the contract on a relative standalone selling price basis, and recognised as revenue at the point at which control of goods or services is transferred to the customer. The transaction price will be the amount of consideration to which the Group expects to be entitled in exchange for transferring promised goods or services to a customer. The incremental costs of obtaining a contract and contract fulfilment costs will be recognised as an expense consistent with the transfer of the related goods or services to the customer. Depending on the particular contractual arrangements in place, application of the new standard may change the amount of revenue recognised on a contract and/or its timing of the recognition of contract costs compared with current accounting policies. An evaluation of its potential impact has commenced but it is too early to determine whether adoption of the standard will have a significant effect on reported results and financial position.

It should be noted that the IASB has indicated that there may be some limited clarifying amendments made to the standard before it becomes fully applicable in the future. The directors will continue to monitor the extent of proposed changes from the IASB and, subject to a detailed review, will update the relevant policy in conjunction with guidance from the Audit Committee and following discussions with the Group's auditor.

3. Significant accounting policies

Basis of accounting

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU, and therefore the Group financial statements comply with Article 4 of the EU IAS Regulation.

The consolidated financial statements have been prepared on the historical cost basis modified by revaluation of certain financial instruments. Historical cost is generally based on the fair value of the consideration given in exchange for goods and services. The consolidated financial statements have been prepared on the going concern basis as detailed in the Directors' Report. The principal accounting policies adopted are set out below.

Basis of consolidation

The consolidated financial statements incorporate the Group and entities controlled by the Group (its subsidiaries) made up to 31 March each year. Control is achieved when the Group:

- has the power over the investee;
- is exposed, or has rights, to variable return from its involvement with the investee; and
- has the ability to use its power to affect its returns.

The Group reassesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control listed above. When the Group has less than a majority of the voting rights of an investee, it considers that it has power over the investee when the voting rights are sufficient to give it the practical ability to direct the relevant activities of the investee unilaterally.

The Group considers all relevant facts and circumstances in assessing whether or not the Group's voting rights in an investee are sufficient to give it power, including:

- the size of the Group's holding of voting rights relative to the size and dispersion of holdings of the other vote holders;
- potential voting rights held by the Group, other vote holders or other parties;
- rights arising from other contractual arrangements; and
- any additional facts and circumstances that indicate that the Group has, or does not have, the current ability to direct the relevant activities at the time that decisions need to be made, including voting patterns at previous shareholders' meetings.

Consolidation of a subsidiary begins when the Group obtains control over the subsidiary and ceases when the Group loses control of the subsidiary. Specifically, the results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the date the Group gains control until the date when the Group ceases to control the subsidiary.

Where necessary, adjustments are made to the consolidated financial statements of subsidiaries to bring the accounting policies used into line with the Group's accounting policies. All intragroup assets and liabilities, equity, income, expenses and cash flows relating to transactions between the members of the Group are eliminated on consolidation.

Revenue

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured, regardless of when payment is being made. Revenue is measured at the fair value of the consideration received or receivable, taking into account contractually defined terms of payment and excluding applicable taxes or duty.

Revenue from the Group's activities is recognised as follows:

Service revenue

Time and materials contracts

Contracts for the provision of services generally tend to be 'time and materials' contracts whereby the customer is contractually bound to pay for services for each hour or day spent in delivering a contractually agreed services scope. These contracts typically have no payment milestones, refunds or bundling with other services or products. Revenue is therefore recognised in line with the chargeable 'time and materials' which are allocated to the contracted project.

Fixed price contracts

When the outcome of a fixed price contract can be estimated reliably, revenue and costs are recognised by reference to the stage of completion. This is normally measured by the proportion of contract costs incurred for work performed to date against the estimated total contract costs. This is reviewed on a monthly basis.

Support and maintenance

Support and maintenance fees are recognised on a straight line basis over the contracted term in line with the estimated delivery of performance obligations.

Third party goods

Revenue from the sale of goods is recognised when the significant risks and rewards of ownership of the goods have passed to the buyer, usually on delivery of the goods.

Perpetual licence income

Licences charged to customers for the use of proprietary software are assessed on a contract by contract basis and depending on the terms, revenue is recognised on a straight line basis during the licence implementation period.

Software as a Service (SaaS)

SaaS is charged on a subscription basis and the revenue is recognised pro-rata over the period that the service is provided.

Leases

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

The Group as lessee

Rentals payable under operating leases are charged to the statement of comprehensive income on a straight line basis over the term of the relevant lease except where another more systematic basis is more representative of the time pattern in which economic benefits from the lease asset are consumed. Contingent rentals arising under operating leases are recognised as an expense in the period in which they are incurred. In the event that lease incentives are received to enter into operating leases, such incentives are recognised as a liability. The aggregate benefit of incentives is recognised as a reduction of rental expense on a straight line basis over the lease term, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed.

Notes to the consolidated financial statements continued

Foreign currencies
The individual financial statements of each Group entity are presented in the currency of the primary economic environment in which it operates (its functional currency). For the purpose of the consolidated financial statements, the results and financial position of each Group entity are expressed in Pounds Sterling, which is the presentation currency for the consolidated financial statements.

In preparing the financial statements of the individual companies, transactions in currencies other than the entity's functional currency (foreign currencies) are recognised at the rates of exchange prevailing on the dates of the transactions. At each statement of financial position date, monetary assets and liabilities that are denominated in foreign currencies are retranslated at the rates prevailing at that date. Non-monetary items carried at fair value that are denominated in foreign currencies are translated at the rates prevailing at the date when the fair value was determined.

Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated. Exchange differences are recognised in the statement of comprehensive income in the period in which they arise, except for exchange differences on monetary items receivable from or payable to a foreign operation for which settlement is neither planned nor likely to occur in the foreseeable future (therefore forming part of the net investment in the foreign operation), which are recognised initially in other comprehensive income and reclassified from equity to profit or loss on disposal or partial disposal of the net investment.

For the purpose of presenting consolidated financial statements, the assets and liabilities of the Group's foreign operations are translated at exchange rates prevailing on the statement of financial position date. Income and expense items are translated at the average exchange rates for the period, unless exchange rates fluctuate significantly during that period, in which case the exchange rates at the date of transactions are used. Exchange differences arising, if any, are recognised in other comprehensive income and accumulated in equity (attributed to non-controlling interests as appropriate).

Government grants
Government grants are not recognised until there is reasonable assurance that the Group will comply with the conditions attaching to them and that the grants will be received.

Government grants are generally recognised in the statement of comprehensive income on a systematic basis over the periods in which the Group recognises as expenses the related costs for which the grants are intended to compensate. Specifically, government grants whose primary condition is that the Group should purchase non-current assets are recognised as deferred revenue in the statement of financial position and transferred to the statement of comprehensive income on a systematic and rational basis over the useful lives of the related assets. Other grants are credited to the statement of comprehensive income when there is reasonable assurance the grant conditions have been complied with and that the grant money will be received.

Retirement benefit costs
The Group operates two defined contribution pension schemes and the pension charge represents the amounts payable by the Group to the funds in respect of the year. Differences between contributions payable in the year and contributions actually paid are shown as either accruals or prepayments in the statement of financial position.

Taxation
The tax expense represents the sum of the tax currently payable and deferred tax.

Current tax
The tax currently payable is based on taxable profit for the year. Taxable profit differs from net profit as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the statement of financial position date.

Current tax is recognised in the statement of comprehensive income, except when it relates to items that are recognised in other comprehensive income or directly in equity, in which case, the current tax is also recognised in other comprehensive income or directly in equity respectively.

Deferred tax
Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the consolidated financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries and associates, and interests in joint ventures, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets arising from deductible temporary differences associated with such investments and interests are only recognised to the extent that it is probable that there will be sufficient taxable profits against which to utilise the benefits of the temporary differences and they are expected to reverse in the foreseeable future. The carrying amount of deferred tax assets is reviewed at each statement of financial position date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised based on tax laws and rates that have been enacted or substantively enacted at the statement of financial position date. Deferred tax is charged or credited in the statement of comprehensive income, except when it relates to items charged or credited in other comprehensive income, in which case the deferred tax is also dealt with in other comprehensive income.

The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Group expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis.

RDEC
The Group has adopted the Research and Development Expenditure Credit regime (RDEC). As a result, research and development tax credits previously reported within the income tax expense are replaced by research and development grants and are offset against operating expenses. RDEC grant amounts are recognised as and when certainty over related conditions have been met and the grant amounts will be received. A corresponding other receivable is recognised at the time the grants are earned and will subsequently be offset against tax payable.

Property, plant and equipment
Property, plant and equipment assets are stated at cost, net of depreciation and any provision for impairment. Depreciation is provided at rates calculated to write off the cost less residual value of each asset on a straight line basis, over its expected life.

The principal annual rates are as follows:

Long term leasehold property	2.5%
Short term leasehold property	Over the term of the lease
Fixtures and fittings	20%
Office equipment	33%

The estimated useful lives, residual values and depreciation method are reviewed at the end of each reporting period, with the effect of any changes in estimate accounted for on a prospective basis.

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. The gain or loss arising on the disposal or scrappage of an asset is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in the statement of comprehensive income.

Loans and receivables
Trade receivables, loans and other receivables that have fixed or determinable payments not quoted in an active market are classified as 'loans and receivables'. Loans and receivables are measured at amortised cost using the effective interest method, less any impairment. Interest income is recognised by applying the effective interest rate, except for short term receivables when the recognition of interest would be immaterial.

Share-based payments
Equity-settled share-based payments to employees are measured at the fair value of the equity instruments at the grant date. The fair value excludes the effect of non-market-based vesting conditions. Details regarding the determination of the fair value of equity-settled share-based transactions are set out in note 21.

Where the Company has granted rights to its equity instruments to employees of other Group companies, such arrangements are accounted for as equity-settled share-based payment arrangements. A capital contribution is recognised in the subsidiary company accounts to the extent that they are not recharged with a corresponding increase in the investment in the subsidiary held by the Company.

The fair value determined at the grant date of the equity-settled share-based payments is expensed on a straight line basis over the vesting period, based on the Group's estimate of equity instruments that will eventually vest.

At each statement of financial position date, the Group revises its estimate of the number of equity instruments expected to vest as a result of the effect of non-market-based vesting conditions. The impact of the revision of the original estimates, if any, is recognised in profit or loss such that the cumulative expense reflects the revised estimate, with a corresponding adjustment to equity reserves.

Internally generated intangible assets – research and development expenditure
Expenditure on research activities is recognised as an expense in the period in which it is incurred.

An internally generated intangible asset arising from development (or from the development phase of an internal project) is recognised if all of the following conditions have been demonstrated:

- the technical feasibility of completing the intangible asset so that it will be available for use or sale;
- the intention to complete the intangible asset and use or sell it;
- the ability to use or sell the intangible asset;
- how the intangible asset will generate probable future economic benefits;
- the availability of adequate technical, financial and other resources to complete the development and to use or sell the intangible asset; and
- the ability to measure reliably the expenditure attributable to the intangible asset during its development.

The amount initially recognised for internally generated intangible assets is the sum of the expenditure incurred from the date when the intangible asset first meets the recognition criteria listed above. Where no internally generated intangible asset can be recognised, development expenditure is recognised in profit or loss in the period in which it is incurred.

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 the Group will be required to settle that obligation and a reliable estimate can be made of the amount of the obligation.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at the statement of financial position date, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows (when the effect of the time value of money is material).

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, a receivable is recognised as an asset if it is virtually certain that reimbursement will be received and the amount of the receivable can be measured reliably.

Onerous contracts
Present obligations arising under onerous contracts are recognised and measured as provisions. An onerous contract is considered to exist where the Group has a contract under which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it.

Exceptional items
Exceptional items are disclosed separately in note 8. Due to the materiality, nature and infrequency of the events giving rise to these exceptional items, they merit separate presentation to allow shareholders to understand better the elements of financial performance in the year, so as to facilitate comparison with prior periods and to assess more accurately trends in financial performance. No such exceptional items have occurred in the current year.

4. Material accounting judgements and key sources of estimation uncertainty

In the application of the Group's accounting policies, which are described in note 3, the directors are required to make judgements, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Significant judgements and estimates in applying the Group's accounting policies

In the application of the Group's accounting policies and preparation of financial statements in conformity with IFRSs, management are required to make judgements and estimates that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and other factors considered relevant and take account of the circumstances and facts at the period end. Actual results may differ from these estimates. This summary is not a list of all uncertainties, estimates and judgements encountered and others could arise that cause a material adjustment to the carrying value of assets or liabilities within the next financial year.

(a) Key sources of estimation that have been made that have the most significant effect on the amounts recognised in the consolidated financial statements include:

Revenue recognition

Service revenue

Kainos charges for its digital services on a time and materials or fixed price basis. In 2017, the majority of service revenue (approximately 88%) was derived from time and materials contracts and the remainder from fixed price contracts. Where there are fixed price contracts revenue is recognised based on the stage of completion. Stage of completion is measured by reference to costs incurred to date as a percentage of total estimated costs. The Group estimates costs to complete its contractual obligations by reference to the current run rate of these costs until contractual completion. Estimates can vary as there will be technical issues to overcome, timescales change and there could be commercial issues. Therefore the status of customer contracts are assessed on an ongoing basis.

Perpetual licence income

The Group's Digital Platforms are licensed to customers on a recurring annual basis following a SaaS business model and less frequently as a fixed one-off lifetime perpetual licence (for some Evolve customers). Licences charged to customers for the use of proprietary software are assessed on a contract by contract basis depending on the implementation terms specified in the underlying contract. The implementation period may change due to customer requirements, and as such changes in the estimated implementation period can impact the amount of licence revenue recognised.

RDEC income

Estimates are made in determining the product development expenditure eligible for RDEC. RDEC grants are recognised when there is certainty that related conditions have been met and the grant will be received. The unrecognised RDEC component at 31 March 2017 equates to £2.2 million and appropriate amounts will be released as and when the conditions have been met and the grants in relation to that amount have been received.

Fair values

IFRSs require many assets, liabilities and expenses to be recognised at fair value. Where open market values are not available the fair values are estimates and therefore subject to assumptions. This applies to share-based payments as detailed in note 21.

(b) The significant judgements that have been made that have the most significant effect on the amounts recognised in the consolidated financial statements include:

Product development expenditure

Kainos invests on a continual basis in the development of new and enhanced features in the product suite. There is a continual process of enhancements to and expansion of the overall product suite. Therefore, judgement is required in determining the practice for capitalising development costs. Judgement is required in assessing whether the development costs meet the criteria for capitalisation. These judgements have been applied consistently year to year. The accounting policy for research and product development is in note 3 and in the current year there are no development expenses that have been capitalised. The total product development expenditure in the period is £4.6 million (2016: £2.3 million). Product development expenditure is partially offset against RDEC grants received from HMRC.

Generally, commercial viability of new products is not proven until all high-risk development issues have been resolved through testing pre-launch versions of the product. As a result, technical feasibility is proven only after completion of the detailed design phase and formal approval, which occurs just before the products are ready to go to market. Accordingly, development costs have not been capitalised.

Costs which are incurred after the general release of internally generated software or costs which are incurred in order to enhance existing products are expensed in the period in which they are incurred and included within research and development expense in the financial statements.

Grant income

Government grants are generally recognised in the statement of comprehensive income on a systematic basis over the periods in which the Group recognises as expenses the related costs for which the grants are intended to compensate. Judgement is applied in assessing when there is reasonable assurance the grant conditions have been complied with and that the grant money will be received.

5. Segment reporting

All of the Group's revenue during the period to 31 March 2017 was derived from continuing operations. Kainos is structured into two divisions: Digital Services and Digital Platforms.

Digital Services include full life cycle development and support of digital solutions for government and commercial customers. Kainos is also the largest boutique partner for Workday in Europe, responsible for implementing Workday's innovative Software-as-a-Service (SaaS) platform for enterprise customers.

Digital Platforms comprise Evolve EMR, the market leading product for the digitisation of patient notes in the Acute sector of the NHS; Evolve IC, an integrated care platform for NHS and international healthcare providers; and Smart, an automated testing platform for Workday customers.

To date the Group has presented its results by operating division (Digital, Evolve, WorkSmart). Going forward, the directors consider that presenting its operations in terms of Digital Services and Digital Platforms better represents the Group's business by more clearly highlighting how each offering is positioned in the market, and more easily allowing the application of appropriate performance metrics to each part of the business. This also reflects how the business is managed and reported internally. A full reconciliation between the previous and current segmental reporting is provided in note 25.

Notes to the consolidated financial statements continued

Segment revenue and results

The following is an analysis of the Group's revenue and results by reportable segment:

2017 **12 months to 31 March**	Digital Services (£000s)	Digital Platforms (£000s)	Consolidated (£000s)
Revenue	**64,526**	**18,978**	**83,504**
Cost of sales	**(33,374)**	**(6,594)**	**(39,968)**
GROSS PROFIT	**31,152**	**12,384**	**43,536**
Direct expenses	**(6,186)**	**(10,433)**	**(16,619)**
CONTRIBUTION	**24,966**	**1,951**	**26,917**
Operating expenses excluding share-based payments			**(12,648)**
ADJUSTED PRE-TAX PROFIT			**14,269**

2016 12 months to 31 March	Digital Services (£000s)	Digital Platforms (£000s)	Consolidated (£000s)
Revenue	55,080	21,514	76,594
Cost of sales	(29,705)	(9,780)	(39,485)
GROSS PROFIT	25,375	11,734	37,109
Direct expenses	(5,450)	(6,839)	(12,289)
CONTRIBUTION	19,925	4,895	24,820
Operating expenses excluding share-based payments			(10,719)
ADJUSTED PRE-TAX PROFIT			14,101

Reconciliation of adjusted pre-tax profit to profit before tax

	2017 (£000s)	2016 (£000s)
ADJUSTED PRE-TAX PROFIT	**14,269**	14,101
Share-based payments	**(949)**	(524)
Exceptional items	**–**	684
PROFIT BEFORE TAX	**13,320**	14,261

The Group's revenue from external customers by geographic location is detailed below:

	2017 (£000s)	2016 (£000s)
United Kingdom	**64,879**	65,314
Republic of Ireland	**8,725**	5,371
US	**4,420**	4,005
Other	**5,480**	1,904
	83,504	76,594

The accounting policies of the reportable segments are the same as the Group's accounting policies described in note 3. Segment assets and liabilities are not reported to the chief operating decision maker (CODM) on a segmental basis and therefore are not disclosed.

Significant customer

A Digital Services client ("Customer A") accounted for £10.4 million (or 13%) of total Group revenue during 2017 (2016: £5.8 million or 8%). Another Digital Services client ("Customer B") accounted for £12.8 million (or 15%) of total 2017 Group revenue (2016: £10.3 million or 14%). No other single customer contributed 10% or more to the Group's consolidated revenue during the period to 31 March 2017.

6. Profit for the year

Profit for the year has been arrived at after charging/(crediting):

	2017 (£000s)	2016 (£000s)
Total staff costs (note 7)	**43,747**	35,373
Government grants	**(1,676)**	(426)
Operating lease rentals (note 20)	**1,272**	1,026
Research and development costs	**4,641**	2,332
Research and Development Expenditure Credit grant	**(1,715)**	–
Depreciation of property, plant and equipment (note 12)	**897**	687
Net foreign exchange gains	**(784)**	(412)
Fair value measurement of foreign currency forward contracts (note 23)	**–**	(98)

Kainos has implemented the Research and Development Expenditure Credit regime ("RDEC") during the period and, as a result, research and development grants are offset against operating expenses. In the year to 31 March 2017, RDEC grants have reduced operating expenses by £1.7 million, of which £1.1 million relates to prior periods.

The analysis of auditor's remuneration is as follows:

	2017 (£000s)	2016 (£000s)
Fees payable to the Group's auditor for the audit of the Group's annual accounts	**52**	68
Fees payable to the Group's auditor for the audit of subsidiaries	**32**	20
Total audit fees	**84**	88
Fees payable to the Group's auditor for other services to the Group:		
Review of interim report	**16**	20
Other audit related services	**–**	5
Total audit related fees	**100**	113
Grants assurance services	**–**	14
IPO related	**–**	336
Taxation compliance services	**–**	12
Other taxation advisory services	**–**	13
Total non-audit fees	**–**	375
Total audit and non-audit fees	**100**	488
Total % of non-audit fees	**0%**	77%

Notes to the consolidated financial statements continued

7. Staff numbers and costs

The average number of employees during the year was:

	2017 Number	2016 Number
Technical	**749**	643
Administration	**80**	58
Sales	**55**	32
	884	733

Their aggregate remuneration comprised:

	2017 (£000s)	2016 (£000s)
Wages and salaries	**37,749**	30,238
Social security costs	**4,643**	3,763
Other pension costs	**1,355**	1,372
	43,747	35,373

8. Exceptional items

In 2017 the Group had no exceptional items. In the prior year the Group completed the disposal of its entire shareholding in SpeechStorm for a consideration of £2.0 million, all of which was recognised as an exceptional gain during the prior year. Exceptional expenses in the prior year of £1.3 million related to costs associated with the IPO of Kainos Group plc shares on the London Stock Exchange on 10 July 2015.

9. Tax on ordinary activities

	2017 (£000s)	2016 (£000s)
Corporation tax:		
Current year (UK)	**2,497**	1,723
Current year (overseas)	**377**	496
Adjustments in respect of prior years	**218**	(439)
	3,092	1,780
Deferred tax (note 17)	**(188)**	54
	2,904	1,834

UK corporation tax is calculated at 20% (2016: 20%) of the estimated taxable profit for the year. Taxation for other jurisdictions is calculated at the rates prevailing in the respective jurisdictions. The effective tax rate for 2017 was 22% (2016: 13%). The increase in the effective tax rate is largely due to the impact of research and development credits in 2016 and the exceptional gain on the SpeechStorm sale both reducing the effective tax rate last year. From 1 April 2016 there is a requirement for the Group to move from submitting research and development expenditure related tax claims under the previous large company super deduction scheme (which resulted in additional tax deductions accounted for within the tax charge) to the RDEC scheme (which results in credits accounted for within operating profit).

Changes to the UK corporation tax rates were substantively enacted as part of the Finance Act 2016 and Finance Act 2015. As a result, the main rate of corporation tax reduced to 19% from 1 April 2017 and will reduce to 17% from 1 April 2020. Whilst there is expected to be a reduction in future UK corporation tax rates we expect this to be offset by growth in overseas profits and therefore consider that the sustainable tax rate is likely to be similar to the rate for 2017.

The Group's tax charge can be reconciled to the profit in the statement of comprehensive income as follows:

	2017 (£000s)	2016 (£000s)
Profit before tax on continuing operations	**13,320**	14,261
Tax at the UK corporation tax rate of 20% (2016: 20%)	**2,664**	2,852
Non-deductible expenses	**61**	409
Non-taxable income	**(6)**	(396)
Research and development super deduction	**–**	(472)
Effect of net losses utilised in the period	**–**	9
Effect of non-UK tax rates	**(11)**	(114)
Movement in prior year unrecognised deferred tax asset	**(23)**	–
Adjustments to tax charge in respect of prior years	**201**	(439)
Change in UK tax rates	**18**	(15)
Tax expense for the year	**2,904**	1,834

In addition to the amount charged to the statement of comprehensive income, the following amounts relating to tax have been recognised directly in equity.

	2017 (£000s)	2016 (£000s)
CURRENT TAX		
Excess tax deductions for share-based payments on exercised options	**–**	(917)
Permanent element of stock option deduction	**(12)**	–
DEFERRED TAX		
Change in estimated tax deductions related to share-based payments	**(4)**	107
Adjustments in respect of previous periods	**(39)**	–
Deferred tax on stock option	**190**	–
Total tax recognised directly in equity	**135**	(810)

10. Dividends

	2017 (£000s)	2016 (£000s)
Amounts recognised as distributions to equity holders in the period:		
Interim dividend for 2017 of 1.9p per share	**2,248**	–
Final dividend for 2016 of 4.2p per share	**4,960**	–
Interim dividend for 2016 of 1.8p per share	**–**	2,133
Dividend for 2015 of 2.3p per share	**–**	2,548
Dividend for 2015 of 7.5p per share	**–**	8,628
	7,208	13,309

The proposed final dividend for 2017 is subject to approval by shareholders at the AGM and has not been included as a liability in these financial statements. The final dividend, if approved by shareholders, will be 4.4p and payable on 20 October 2017 to shareholders on the register on 22 September 2017, with an ex-dividend date of 21 September 2017.

11. Earnings per share

Basic earnings per share is calculated by dividing the profit attributable of ordinary shareholders to the parent company by the weighted average number of ordinary shares in issue during the period.

	2017 (£000s)	2016 (£000s)
Profit for the period	**10,416**	12,427

	Thousands	Thousands
Weighted average number of ordinary shares for the purposes of basic earnings per share	**117,200**	115,775
Effect of dilutive potential ordinary shares from share options	**2,773**	1,233
Weighted average number of ordinary shares for the purposes of diluted earnings per share	**119,973**	117,008
Basic earnings per share	**8.9p**	10.7p
Diluted earnings per share	**8.7p**	10.6p

Adjusted basic earnings per share is calculated by dividing the profit attributable to ordinary equity holders of the parent company, excluding exceptional items and share-based payments (including associated taxes) by the weighted average number of ordinary shares in issue during the period.

	2017 (£000s)	2016 (£000s)
Profit for the period	**10,416**	12,427
Exceptional expenses in relation to IPO	**–**	1,297
Exceptional gain on disposal of investment	**–**	(1,981)
Share-based payments (including associated taxes)	**949**	524
Adjusted profit for the period	**11,365**	12,267

	Thousands	Thousands
Weighted average number of ordinary shares for the purposes of basic earnings per share	**117,200**	115,775
Effect of dilutive potential ordinary shares from share options	**2,773**	1,233
Weighted average number of ordinary shares for the purposes of diluted earnings per share	**119,973**	117,008
Adjusted basic earnings per share	**9.7p**	10.6p
Adjusted diluted earnings per share	**9.5p**	10.5p

12. Property, plant and equipment

	Leasehold property (£000s)	Office equipment (£000s)	Fixtures and fittings (£000s)	Total (£000s)
At 1 April 2015	2,545	2,076	1,052	5,673
Additions	–	791	231	1,022
Disposals	–	(271)	–	(271)
At 31 March 2016	2,545	2,596	1,283	6,424
Additions	–	646	167	813
Disposals	–	(52)	–	(52)
At 31 March 2017	**2,545**	**3,190**	**1,450**	**7,185**
Accumulated depreciation				
At 1 April 2015	1,957	1,201	764	3,922
Charge for the year	35	535	117	687
Eliminated on disposals	–	(271)	–	(271)
At 31 March 2016	1,992	1,465	881	4,338
Charge for the year	35	705	157	897
Eliminated on disposals	–	(52)	–	(52)
At 31 March 2017	**2,027**	**2,118**	**1,038**	**5,183**
Carrying amount				
At 31 March 2017	**518**	**1,072**	**412**	**2,002**
At 31 March 2016	553	1,131	402	2,086
At 31 March 2015	588	875	288	1,751

Notes to the consolidated financial statements continued

13. Subsidiaries

The subsidiary undertakings at 31 March 2017 are in the table below. All principally operate in their country of incorporation.

Subsidiary undertakings	Incorporated	Registered office	Principal activity	Proportion of ordinary share capital held
Kainos Software Limited	Northern Ireland	Kainos House, 4-6 Upper Crescent, Belfast, BT7 1NT	Software development	100%
Kainos Software Ireland Limited	Republic of Ireland	6-7 Saint Stephen's Green, Dublin 2	Software development	100%
Kainos Software Poland Spólka z.o.o	Poland	Tryton Business House, ul. Jana z Kolna 11, 80-864 Gdansk	Software development	100%
Kainos Trustees Limited	Northern Ireland	Kainos House, 4-6 Upper Crescent, Belfast, BT7 1NT	Share Scheme Trustee	100%
Kainos Managers Limited	Northern Ireland	Kainos House, 4-6 Upper Crescent, Belfast, BT7 1NT	Dormant	100%
Kainos Evolve Limited	Northern Ireland	Kainos House, 4-6 Upper Crescent, Belfast, BT7 1NT	Software development	100%
Kainos WorkSmart Limited	Northern Ireland	Kainos House, 4-6 Upper Crescent, Belfast, BT7 1NT	Software development	100%
Kainos WorkSmart Inc.	US	470 Atlantic Avenue, 4th Floor, Boston, Massachusetts 02210	Software development	100%
Kainos Evolve Inc.	US	470 Atlantic Avenue, 4th Floor, Boston, Massachusetts 02210	Software development	100%
Kainos Worksmart GmbH	Germany	The Squaire 12, Am Flughafen Hessen, Frankfurt 60549	Software development	100%

There are no significant restrictions on the ability of the Group to access or use assets and settle liabilities. The directors consider that the Group has no ultimate controlling party.

14. Investments

The Group has unlisted investments as follows:

	(£000s)
Cost	
At 31 March 2016 and 2017	**900**
Provision for impairment	
At 31 March 2016 and 2017	**–**
Carrying amount	
At 31 March 2016 and 2017	**900**

In February 2016, the Group acquired 10% of the share capital of Cirdan Imaging Limited, a privately-owned supplier of medical diagnostic hardware and software, incorporated in Northern Ireland, for £0.9 million. Cirdan's wide international presence and its strong credentials in the healthcare industry offers the potential to strengthen significantly the Evolve proposition in new global markets.

The directors consider that the carrying amount of the investment approximates to its fair value.

15. Trade and other receivables

	2017 (£000s)	2016 (£000s)
Trade receivables	**16,168**	14,541
Allowance for doubtful debts	**(15)**	(66)
	16,153	14,475
Other debtors	**882**	573
RDEC grant	**1,715**	–
	18,750	15,048

Included in trade receivables are the following amounts from significant customers listed in note 5 above (Segment Reporting): Customer A – 2017: £3.2 million (2016: £1.4 million) and Customer B – 2017: £1.4 million (2016: £1.6 million). In addition to Customer A and B there is one further customer who represents greater than 5% of the total balance of trade receivables as at 31 March 2017.

The average credit period extended to customers is 30 days. Specific provision on overdue amounts is made based on historical trade with the counterparty and the counterparty's current financial standing.

The Group does not hold any collateral or other credit enhancements over any of its trade receivables nor does it have a legal right of offset against any amounts owed by the Group to the counterparty.

The ageing of the Group's trade debtors which are past due but not impaired is shown below:

	2017 (£000s)	2016 (£000s)
31-60 days	**2,397**	4,029
61-90 days	**539**	971
91+ days	**173**	127
Sub-total	**3,109**	5,127

Notes to the consolidated financial statements continued

The Group's impaired trade debtors at each statement of financial position date were aged as follows:

	2017 (£000s)	2016 (£000s)
91+ days	**15**	66

The movement in the allowance for doubtful debts is shown below:

	2017 (£000s)	2016 (£000s)
Balance at the beginning of the period	**66**	–
Impairment losses recognised	**15**	66
Amounts recovered during the year	**(66)**	–
Balance at the end of the period	**15**	66

In determining the recoverability of a trade receivable the Group considers any change in the credit quality of the trade receivable from the date credit was initially granted up to the reporting date. The concentration of credit risk is limited due to the customer base being large and unrelated.

16. Other non-current assets

	2017 (£000s)	2016 (£000s)
Prepayments	**–**	379
Deferred tax asset (note 17)	**324**	–
	324	379

17. Deferred tax

The following are the major deferred tax liabilities and assets recognised by the Group and movements thereon.

	Accelerated capital allowances (£000s)	Forward contract fair value (£000s)	Share-based payment (£000s)	Tax losses (£000s)	Other (£000s)	Total (£000s)
At 1 April 2015	(113)	19	219	–	7	132
Charge to retained earnings	–	–	(86)	–	–	(86)
(Charge)/credit to profit	(13)	(17)	(49)	–	17	(62)
Effect of change in tax rate in retained earnings	–	–	(20)	–	–	(20)
Effect of change in tax rate in income statement	11	(2)	(2)	–	–	7
At 1 April 2016	(115)	–	62	–	24	(29)
Foreign exchange differences	–	–	–	–	(4)	(4)
(Charge)/credit to retained earnings	–	–	172	–	–	172
(Charge)/credit to profit	38	–	3	19	124	184
Effect of change in tax rate in retained earnings	–	–	(4)	–	–	(4)
Effect of change in tax rate in income statement	6	–	2	–	(3)	5
At 31 March 2017	**(71)**	**–**	**235**	**19**	**141**	**324**

Deferred tax assets and liabilities are offset where the Group has a legally enforceable right to do so. The following is the analysis of the deferred tax balances (after offset) for financial reporting purposes:

	2017 (£000s)	2016 (£000s)
Deferred tax liabilities	**(71)**	(115)
Deferred tax assets	**395**	86
	324	(29)

18. Trade and other payables

	2017 (£000s)	2016 (£000s)
Trade creditors and accruals	**8,683**	7,901
Deferred income	**6,320**	4,218
Corporation tax	**2,075**	–
Other tax and social security	**3,573**	3,637
	20,651	15,756

Trade creditors and accruals principally comprise amounts outstanding for trade purchases and ongoing costs, including payroll. For most suppliers no interest is charged on payables.

Deferred income is analysed as follows:

By type	**2017 (£000s)**	2016 (£000s)
Arising from advance payments	**6,307**	4,194
Arising from government grants	**13**	24
Total deferred income	**6,320**	4,218

The deferred income can arise in respect of support and maintenance contracts billed quarterly or annually in advance and certain licence agreements which are billed annually in advance, with revenue being recognised for both over the licence implementation period.

Other provisions are analysed as follows:

	2017 (£000s)	2016 (£000s)
Property-related provision	**297**	297
Non-current	**297**	297
	297	297

	Property-related provision (£000s)	Total (£000s)
At 1 April 2016	297	297
Additional provision in the year	–	–
Release of provision in the year	–	–
At 31 March 2017	**297**	**297**

The property-related provision represents management's best estimate of the Group's liability for future contractual repair works at the end of the lease period.

19. Share capital and reserves

Share capital

	2017 (£000s)	2016 (£000s)
ISSUED AND FULLY PAID:		
Ordinary shares		
Opening balance	**590**	549
Issued during the year	**2**	41
Total share capital	**592**	590

The Company has one class of ordinary share which carries no right to fixed income. The Company's Articles of Association do not specify any limit on the total authorised share capital of the Company.

At 31 March 2017, the Company has 118,342,144 ordinary shares (2016: 117,995,265) with a nominal value of £0.005 each.

Share premium account

	(£000s)
Balance at 31 March 2016	1,607
Issue of share capital at a premium	19
Balance at 31 March 2017	**1,626**

Capital reserve account

	(£000s)
Balance at 31 March 2016	668
Issue of share capital	(1)
Balance at 31 March 2017	**667**

Retained earnings

	(£000s)
Balance at 31 March 2015	22,606
Deferred tax equity movement	(107)
Current tax equity movement	917
Dividends paid	(13,309)
Profit for the year	12,427
Balance at 31 March 2016	22,534
Deferred tax equity movement	147
Current tax equity movement	(12)
Adjustments in respect of previous periods	194
Dividends paid	(7,208)
Profit for the year	10,416
Balance at 31 March 2017	**26,071**

20. Operating leases

The Group as a lessee

	2017 (£000s)	2016 (£000s)
Lease payments recognised as an expense in the year	**1,272**	1,026

The Group had outstanding commitments for future minimum lease payments under non-cancellable operating leases, which fall due as follows:

	2017 (£000s)	2016 (£000s)
Within one year	**854**	940
In the second to fifth years inclusive	**1,212**	1,443
Greater than five years	**202**	444
	2,268	2,827

Operating lease payments represent rentals payable by the Group for certain of its office properties and vehicles. The Group's property leases cover its offices and the apartments required to deliver customer projects. The lease terms vary in duration and are all priced at prevailing market rate.

21. Share-based payments

The Group has the following share schemes:

Kainos Group Performance Share Plan

Share options are granted to employees as determined by the Remuneration Committee and will only vest in accordance with the performance conditions established by the Committee. The options cannot generally be exercised within three years and have a maximum life of ten years. The options will be settled by the issue of new shares and there are no cash settlement alternatives.

Company Share Option Plan

Share options are granted to employees as determined by the Remuneration Committee. The CSOP is a sub-plan of the PSP and permits the Company to grant CSOP options which have tax advantages pursuant to the provisions of Schedule 4 to the Income Tax (Earnings & Pensions) Act 2003 ("Schedule 4"). The options cannot be ordinarily exercised within three years and have a maximum life of ten years. Exercise of the options will be settled by the issue of shares and there are no cash alternatives.

SAYE Scheme

The Group has an all-employee share plan open to UK employees. To date there has been only one grant under this scheme. Under the scheme, employees who participate have entered into a savings contract under which they agree to save between £5 and £100 per month (or such limit as may be permitted by the tax legislation governing SAYE schemes from time to time) for three years. Options cannot be ordinarily exercised within three years and must be exercised within six months of the end of the three-year period.

Republic of Ireland Share Option Scheme

The Group has a share option scheme for employees of Kainos Software Ireland Limited. This scheme utilised the PSP Scheme to grant options to all eligible employees. Options cannot be ordinarily exercised within three years and must be exercised within six months of the end of the three year period. The options will be settled by shares and there are no cash alternatives.

UK Share Incentive Plan (SIP)

The Group has established a Share Incentive Plan for UK employees. Under this scheme all eligible employees are awarded a number of shares determined by length of service of each employee at a specified date for each respective grant. The shares are held in trust for each employee by Yorkshire Building Society, which also administers the scheme. The vesting period for these shares is three years.

Republic of Ireland Restricted Share Scheme

The Group introduced a Restricted Share Scheme for all eligible employees of Kainos Software Ireland Limited. Under this scheme all eligible employees were awarded a number of shares determined by length of service of each employee employed as at 30 June 2015. The vesting period for these shares is five years and one week and the shares are not accessible by the employee until expiry of that period. The shares are held in trust for the employees until they vest.

Kainos Group plc Poland Share Plans

In order to replicate the share-based awards available to staff in the UK and Ireland, the Group implemented the Kainos Group plc Poland Share Plan. The Remuneration Committee may grant Share Options or Conditional Share Awards to employees of the Group Polish subsidiary. Share options will not generally be exercisable within three years and have a maximum life of 10 years. Conditional Share Awards may be granted for free or at a purchase price determined by the Committee. Conditional Share Awards will generally be subject to a minimum three year vesting period. All options and awards will be satisfied out of newly issued shares and there are no cash settlement alternatives.

Fair values and awards outstanding

For share awards under the PSP, CSOP and ROI share option schemes, the fair value has been measured using the Black-Scholes model. In the absence of historic volatility data, expected volatility has been estimated using the volatility rates of comparable companies.

PSP	Granted in 2017	Granted in 2016
Fair value	£1.38	£0.43-£1.22
Share price at grant	£1.62	£1.39
Expected volatility	30%	30%
Expected life (years)	3.5	3.5
Expected dividends per annum	3.08%	3.69%

CSOP	Granted in 2017	Granted in 2016
Fair value	£0.28-£0.38	£0.22-£0.37
Share price at grant	£1.62-£2.06	£1.39-£2.31
Expected volatility	30%	30%
Expected life (years)	3.5	3.5
Expected dividends per annum	3.08%	3.69%

UK SAYE	Granted in 2017	Granted in 2016
Fair value	–	£0.33
Share price at grant	–	£1.39
Expected volatility	–	30%
Expected life (years)	–	3.25
Expected dividends per annum	–	3.69%

ROI share options	Granted in 2017	Granted in 2016
Fair value	–	£0.83
Share price at grant	–	£2.09
Expected volatility	–	30%
Expected life (years)	–	3.25
Expected dividends per annum	–	3.69%

Poland share options	Granted in 2017	Granted in 2016
Fair value	£0.72	–
Share price at grant	£1.90	–
Expected volatility	30%	–
Expected life (years)	3.5	–
Expected dividends per annum	2.63%	–

Restricted shares	UK SIP (000s)	ROI (000s)	Poland conditional share awards (000s)	Total (000s)
Outstanding at 31 March 2016	697	34	–	731
Granted during period	323	10	285	618
Forfeited during the period	(67)	(1)	(14)	(82)
Outstanding at 31 March 2017	**953**	**43**	**271**	**1,267**

	PSP (000s)	CSOP (000s)	UK SAYE (000s)	ROI share options (000s)	Poland share options (000s)	Total (000s)
Outstanding at 31 March 2016	1,184	849	1,046	58	–	3,137
Granted during period	610	209	–	–	336	1,155
Forfeited during the period	–	(49)	(65)	(3)	–	(117)
Outstanding at 31 March 2017	**1,794**	**1,009**	**981**	**55**	**336**	**4,175**

The Group recognised total expenses of £0.9 million related to equity-settled share-based payment transactions during the year (2016: £0.5 million).

22. Pensions

The Group operates two defined contribution retirement benefit schemes. The assets of the schemes are held separately from those of the Group in independently administered funds under the control of trustees. The total cost charged to the statement of comprehensive income of £1.4 million (2016: £1.4 million) represents contributions payable to these funds by the Group at rates specified in the rules of the schemes. As at 31 March 2017, contributions of £0.5 million (2016: £0.2 million) were payable to the funds and are included in trade creditors and accruals (note 18).

23. Financial instruments

Capital risk management

The Group manages its capital to ensure that all Group entities will be able to continue as going concerns while maximising the return to shareholders. The Group's overall strategy remained unchanged throughout the period 1 April 2016 to 31 March 2017. The capital structure of the Group consists of Company equity only (comprising issued capital, reserves and retained earnings). The Group is not subject to any externally imposed capital requirements and has no borrowings.

Financial risk management objectives

The Group's Corporate Treasury function provides services to the business, manages and forecasts cash balances on each bank account held and researches available facilities and reports to the CFO on the financial risks relating to the operations of the Group. These risks include market (including currency risk and price risk), credit and liquidity risk.

The use of financial derivatives is governed by the Group's policies approved by the Board, which provide written principles on foreign exchange risk, the use of financial derivatives and non-derivative financial instruments, and the investment of excess liquidity. Compliance with policies and exposure limits is reviewed by the CFO and the Finance function on a continuous basis. The Group does not enter into or trade financial instruments, including derivative financial instruments, for speculative purposes.

The Finance function reports to the Group's Audit Committee which monitors risks and policies implemented to mitigate risk exposures.

Foreign currency risk

The Group's activities expose it to changes in foreign currency exchange rates. This risk is measured through the Group's budgeting and cash flow forecasting processes which identify net foreign currency exposures in Polish Zloty, Euro and US Dollars. The Finance function quantifies and suggests risk mitigation measures to manage the risk in accordance with Group policies and obtains CFO approval for implementation of these risk mitigation procedures.

There has been no change to the nature of market risk which the Group was exposed to during the year, but consistent with the overall growth of the Group's business, the value of this exposure has increased in absolute size, as shown below.

The carrying amounts of the Group's foreign currency denominated monetary assets and monetary liabilities at 31 March 2017 are as follows:

	Liabilities		Assets	
	2017 (£000s)	2016 (£000s)	**2017 (£000s)**	2016 (£000s)
Polish Zloty	**1,288**	886	**785**	210
Euro	**337**	351	**4,589**	3,161
US Dollar	**107**	88	**3,029**	2,139

Foreign currency sensitivity analysis

The Group is mainly exposed to the currency of Poland (Polish Zloty currency), Ireland (Euro currency) and the US (US Dollar currency). The following table details the Group's profit and loss sensitivity to a 1% increase in Sterling against the relevant foreign currencies. 1% is the sensitivity rate used when considering foreign currency risk internally by key management personnel. The sensitivity analysis includes only outstanding foreign currency denominated monetary items and adjusts their translation at the period end for a 1% change in foreign currency rates. A positive number below indicates an increase in profit and other equity where Sterling strengthens 1% against the relevant currency. For a 1% weakening of Sterling against the relevant currency, there would be a comparable impact on the profit and other equity and the balances below would be negative:

	Euro impact		PLN impact		USD impact	
	2017 (£000s)	2016 (£000s)	**2017 (£000s)**	2016 (£000s)	**2017 (£000s)**	2016 (£000s)
1% increase in strength of Sterling	**43**	28	**(5)**	(7)	**29**	21

Forward foreign exchange contracts

The Group may enter into forward foreign exchange contracts to manage the risk associated with anticipated costs for a period up to 12 months.

There were no forward contracts entered into during the year and subsequently there are no outstanding forward contracts at 31 March 2017.

The Group does not currently hedge expected future revenue denominated in Euro or US Dollars as the net exposure is not material to the Group's financial performance or position.

Interest rate risk management

The Group's exposures to interest rates on financial assets are detailed in the liquidity risk management section of this note. The Group's exposure to interest rate risk is immaterial to its financial performance and position given that no external borrowings are held and bank deposit interest income amounted to £66,000 during the year ended 31 March 2017.

Credit risk management

Credit risk refers to the risk that a counterparty will default on its contractual obligations resulting in financial loss to the Group. The Group has adopted a policy of only dealing with creditworthy counterparties, as a means of mitigating the risk of financial loss from defaults. The Group only transacts with entities that are rated the equivalent of investment grade and above, many of whom are UK government public sector bodies. The Group uses publicly available financial information and its own trading records to rate its major customers.

In addition to Customer A and Customer B (noted as significant customers in note 5 – Segment Reporting), there is only one further customer that represents greater than 5% of the total balance of trade receivables as at 31 March 2017.

The credit risk on liquid funds is limited because the counterparties are banks with high credit ratings assigned by international credit rating agencies. The Group's exposure and the credit ratings of its counterparties are continuously monitored and the aggregate value of transactions concluded is spread amongst approved counterparties. Credit exposure is controlled by counterparty limits that are reviewed and approved by the CFO in line with Group policies. The expected maturity of the financial assets and liabilities is the same as the reported contractual maturity.

Notes to the consolidated financial statements continued

Liquidity risk management

Ultimate responsibility for liquidity risk management rests with the Board, which has established an appropriate liquidity risk management framework for the management of the Group's short, medium and long term funding and liquidity management requirements. The Group manages liquidity risk by maintaining adequate cash reserves and banking facilities and by matching the maturity profiles of financial assets and liabilities.

The Group's bank deposits all mature within three months of placement. The interest rates obtained on these deposits during the year were variable and attracted interest at below 1% per annum. All other cash balances are instantly accessible.

The Group expects to meet its obligations from existing cash balances and future operating cash flows.

24. Related party transactions

Balances and transactions between the Company and its subsidiaries, which are related parties, have been eliminated on consolidation and are not disclosed in this note.

Trading transactions

During the year, Group companies entered into the following transactions with related parties who are not members of the Group:

	Sale of goods and services		Purchase of goods and services	
	2017 (£000s)	2016 (£000s)	**2017 (£000s)**	2016 (£000s)
Cirdan Imaging Limited	**991**	781	**–**	–
Queen's University Belfast	**–**	–	**301**	312
Total	**991**	781	**301**	312

The following amounts were outstanding at the state of financial position date:

	Amounts owed by related parties		Amounts owed to related parties	
	2017 (£000s)	2016 (£000s)	**2017 (£000s)**	2016 (£000s)
Cirdan Imaging Limited	**390**	283	**5**	–
Queen's University Belfast	**–**	–	**–**	28

Queen's University Belfast is a related party as one of the Group's material shareholders.

Cirdan Imaging Limited is a related party due to the Group's purchase of 10% of its share capital in February 2016.

Remuneration of key management personnel

The remuneration of the directors, who are the key management personnel of the Group, is set out below in aggregate for each of the categories specified in IAS24 Related Party Disclosures.

	2017 (£000s)	2016 (£000s)
Short term employee benefits (emoluments)	**1,168**	1,448
Post-employment benefits (pension contributions)	**29**	27
Share-based payments	**174**	96
	1,371	1,571

One director is a member of the Group's defined contribution pension schemes (2016: one). No directors exercised options over shares in the Company (2016: one). Remuneration of the highest paid director was £459,000 (2016: £501,000), including pension contributions of £29,000 (2016: £27,000). The highest paid director did not exercise any share options in the year (2016: none).

Aggregate directors' remuneration

	2017 (£000s)	2016 (£000s)
Salaries, fees, bonuses and benefits in kind	**1,168**	1,448
Gains on exercise of share options	**–**	4,079
Amounts receivable under long term incentives schemes	**174**	96
Money purchase pension contributions	**29**	27
	1,371	5,650

25. Impact of change in segmental reporting on financial years

Previous Segmental

2017	Digital Services (£000s)	Evolve (£000s)	Workday Smart (£000s)	Workday Services (£000s)	Work-Smart (£000s)	Consolidated (£000s)
Revenue	54,553	14,254	4,724	9,973	14,697	83,504
Cost of sales	(29,150)	(5,516)	(1,078)	(4,224)	(5,302)	(39,968)
Gross profit	**25,404**	**8,738**	**3,646**	**5,748**	**9,394**	**43,536**

Operating expenses excluding share-based payments	**(29,267)**
Share-based payments	(949)
Operating expenses	**(30,216)**
Operating profit	**13,320**

2016	Digital Services (£000s)	Evolve (£000s)	Workday Smart (£000s)	Workday Services (£000s)	Work-Smart (£000s)	Consolidated (£000s)
Revenue	48,504	19,070	2,444	6,576	9,020	76,594
Cost of sales	(26,631)	(8,950)	(830)	(3,074)	(3,904)	(39,485)
Gross profit	**21,873**	**10,120**	**1,614**	**3,502**	**5,116**	**37,109**

Operating expenses excluding share-based payments	**(23,050)**
Share-based payments	(524)
Operating expenses	**(23,574)**
Operating profit before exceptional items	**13,535**

New Segmental

2017	Digital Services (£000s)	Workday Services (£000s)	Services (£000s)	Evolve (£000s)	Workday Smart (£000s)	Platform (£000s)	Consolidated (£000s)
Revenue	54,553	9,973	64,526	14,254	4,724	18,978	83,504
Cost of sales	(29,150)	(4,224)	(33,374)	(5,516)	(1,078)	(6,594)	(39,968)
Gross profit	**25,404**	**5,748**	**31,152**	**8,738**	**3,646**	**12,384**	**43,536**
Direct expenses			(6,186)			(10,433)	(16,619)
Central expenses							(12,648)
Operating expenses excluding share-based payments							**(29,267)**
Share-based payments							(949)
Operating expenses							**(30,216)**
Operating profit							**13,320**

2016	Digital Services (£000s)	Workday Services (£000s)	Services (£000s)	Evolve (£000s)	Workday Smart (£000s)	Platform (£000s)	Consolidated (£000s)
Revenue	48,504	6,576	55,080	19,070	2,444	21,514	76,594
Cost of sales	(26,631)	(3,074)	(29,705)	(8,950)	(830)	(9,780)	(39,485)
Gross profit	**21,873**	**3,502**	**25,375**	**10,120**	**1,614**	**11,734**	**37,109**
Direct expenses			(5,450)			(6,839)	(12,289)
Central expenses							(10,762)
Operating expenses excluding share-based payments							**(23,050)**
Share-based payments							(524)
Operating expenses							**(23,574)**
Operating profit before exceptional items							**13,535**

Notes to the consolidated financial statements continued

Previous Segmental

2015	Digital Services (£000s)	Evolve (£000s)	Workday Smart (£000s)	Workday Services (£000s)	Work-Smart (£000s)	Consolidated (£000s)
Revenue	43,580	9,018	973	7,207	8,180	60,778
Cost of sales	(20,510)	(4,314)	(347)	(3,158)	(3,505)	(28,329)
Gross profit	**23,070**	**4,704**	**626**	**4,049**	**4,675**	**32,449**

Operating expenses	**(20,646)**
Operating profit	**11,803**

2014	Digital Services (£000s)	Evolve (£000s)	Workday Smart (£000s)	Workday Services (£000s)	Work-Smart (£000s)	Consolidated (£000s)
Revenue	31,796	5,948	17	4,154	4,171	41,915
Cost of sales	(15,507)	(2,486)	–	(2,453)	(2,453)	(20,446)
Gross profit	**16,289**	**3,462**	**17**	**1,701**	**1,718**	**21,469**

Operating expenses	**(14,440)**
Operating profit	**7,029**

New Segmental

2015	Digital Services (£000s)	Workday Services (£000s)	Services (£000s)	Evolve (£000s)	Workday Smart (£000s)	Platform (£000s)	Consolidated (£000s)
Revenue	43,580	7,207	50,787	9,018	973	9,991	60,778
Cost of sales	(20,510)	(3,158)	(23,668)	(4,314)	(347)	(4,661)	(28,329)
Gross profit	**23,070**	**4,049**	**27,119**	**4,704**	**626**	**5,330**	**32,449**
Direct expenses			(4,529)			(4,124)	(8,653)
Central expenses							(11,993)
Operating expenses							**(20,646)**
Operating profit							**11,803**

2014	Digital Services (£000s)	Workday Services (£000s)	Services (£000s)	Evolve (£000s)	Workday Smart (£000s)	Platform (£000s)	Consolidated (£000s)
Revenue	31,796	4,154	35,950	5,948	17	5,965	41,915
Cost of sales	(15,507)	(2,453)	(17,960)	(2,486)	–	(2,486)	(20,446)
Gross profit	**16,289**	**1,701**	**17,990**	**3,462**	**17**	**3,479**	**21,469**
Direct expenses			(3,811)			(1,722)	(5,534)
Central expenses							(8,906)
Operating expenses							**(14,440)**
Operating profit							**7,029**

Company statement of financial position

as at 31 March 2017

	Note	**2017 (£000s)**	2016 (£000s)
NON-CURRENT ASSETS			
Investments in subsidiaries	4	**6,524**	6,524
Deferred tax		**62**	43
		6,586	6,567
CURRENT ASSETS			
Debtors	5	**19,936**	12,104
Cash at bank and in hand		**338**	1,690
		20,274	13,794
CREDITORS: AMOUNTS FALLING DUE WITHIN ONE YEAR	6	**(5,266)**	(5,135)
NET CURRENT ASSETS		**15,008**	8,659
TOTAL ASSETS LESS CURRENT LIABILITIES		**21,594**	15,226
NET ASSETS		**21,594**	15,226
CAPITAL AND RESERVES			
Called up share capital	7	**592**	590
Share premium account	7	**1,626**	1,607
Share-based payments reserve	7	**1,279**	524
Capital reserve	8	**5,939**	5,940
Profit and loss account	9	**12,158**	6,565
SHAREHOLDERS' FUNDS		**21,594**	15,226

As permitted by section 408 of the Companies Act 2006, the parent company has elected not to present its own profit and loss account for the year. The parent company reported a profit for the year of £0.3 million (prior period of incorporation 7 May 2015 to 31 March 2016, profit of £8.7 million).

The financial statements of Kainos Group plc (registered number 09579188) were approved by the Board of Directors and authorised for issue on 26 May 2017. They were signed on its behalf by:

Richard McCann
Director
26 May 2017

Company statement of changes in equity

	Equity attributable to equity holders of the Company					
	Share capital (£000s)	Share premium account (£000s)	Share-based payments (£000s)	Capital reserve (£000s)	Retained earnings (£000s)	Total equity (£000s)
Balance at 31 March 2016[1]	590	1,607	524	5,940	6,565	15,226
Issue of share capital (note 7)	2	19	–	(1)	–	20
Share-based payments (note 7)	–	–	949	–	–	949
Adjustments in respect of previous periods	–	–	(194)	–	194	–
Deferred tax for equity-settled share-based payments	–	–	–	–	6	6
Profit and total comprehensive income	–	–	–	–	302	302
Dividends received	–	–	–	–	5,091	5,091
Balance at 31 March 2017	**592**	**1,626**	**1,279**	**5,939**	**12,158**	**21,594**

1 The Company was incorporated on 7 May 2015 as Kainos Group Limited and reregistered as Kainos Group plc on 7 July 2015.

Notes to the Company financial statements

1. Significant accounting policies

The separate financial statements of the parent company are presented as required by the Companies Act 2006. The parent company meets the definition of a qualifying entity under FRS100 (Financial Reporting Standard 100) issued by the Financial Reporting Council. Accordingly, the financial statements have therefore been prepared in accordance with FRS101 (Financial Reporting Standard 101) 'Reduced Disclosure Framework' as issued by the Financial Reporting Council and the recognition and measurement criteria of IFRS as adopted by the EU.

As permitted by FRS101, the parent company has taken advantage of the disclosure exemptions available under that standard in relation to share-based payments, financial instruments, capital management, presentation of a cash flow statement and certain related party transactions.

Where required, equivalent disclosures are given in the consolidated financial statements.

The financial statements have been prepared on the historical cost basis. The principal accounting policies adopted are the same as those set out in note 3 to the consolidated financial statements.

2. Profit for the year

As permitted by section 408 of the Companies Act 2006, the parent company has elected not to present its own profit and loss account for the year. The parent company reported a profit for the year of £0.3 million (prior period of incorporation 7 May 2015 to 31 March 2016, profit of £8.7 million).

The auditor's remuneration for audit and other services is disclosed in note 6 to the consolidated financial statements.

3. Staff numbers and costs

All individuals remunerated by the Company are directors and Non-Executive Directors of the Group, and all remuneration disclosures are made in the Remuneration Report.

4. Investments in subsidiaries

Cost	(£000s)
At 31 March 2016 and 31 March 2017	**6,524**
PROVISIONS FOR IMPAIRMENT	
At 31 March 2016 and 31 March 2017	**–**
CARRYING AMOUNT	
At 31 March 2016 and 31 March 2017	**6,524**

Details of the Group's subsidiaries at 31 March 2017 are included in note 13.

5. Debtors

	2017 (£000s)	2016 (£000s)
AMOUNTS FALLING DUE WITHIN ONE YEAR:		
Amounts owed from Group undertakings	**19,936**	12,104
	19,936	12,104

Amounts owed from other Group companies are repayable on demand, unsecured and carry interest of 5% per annum charged on the average outstanding loan balances.

6. Creditors: Amounts falling due within one year

	2017 (£000s)	2016 (£000s)
Amounts owed to Group undertakings	**4,467**	4,263
Trade creditors and accruals	**678**	773
Corporation tax	**86**	60
Other tax and social security	**35**	39
	5,266	5,135

Amounts owed to other Group companies are repayable on demand, unsecured and carry interest of 5% per annum charged on the average outstanding loan balances.

7. Share capital, share-based payments and share premium accounts

The movements on these items are disclosed in note 19 of the consolidated financial statements.

8. Capital reserve

The movements in the reserve are disclosed in note 19 of the consolidated financial statements.

9. Profit and loss account

	2017 (£000s)	2016 (£000s)
Opening balance	**6,565**	–
Dividends received/(paid)	**5,091**	(2,133)
Deferred tax equity movement	**6**	1
Current tax equity movement	**–**	23
Adjustments in respect of previous periods	**194**	–
Profit for the period	**302**	8,674
	12,158	6,565

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