



**Annual
Report
2015**

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Chairman's Letter



The US presents a major opportunity and it is fitting that preparations for launch are well underway



I am delighted to present the Company's first annual report to investors. It has been an amazing journey, watching AeroForm® grow from a concept to a commercially available product making a difference in the lives of women whose lives have been touched by breast cancer.

AirXpanders had an exciting year in 2015: we listed on the Australian Securities Exchange (ASX) following an oversubscribed Initial Public Offering, we published overwhelmingly positive trial results, commenced the commercial launch of AeroForm Tissue Expander in our first market of Australia, and filed a de novo application for regulatory approval for the AeroForm with the US Food and Drug Administration (FDA).

In the first six months since launching in Australia, AeroForm has had strong uptake from physicians and patients. This is an outstanding achievement and is a testament to the benefits of the AeroForm technology, and the ability of the team to effectively respond to physician and patient demand.

In August, we reported that our pivotal U.S. XPAND trial met its primary endpoint of successful exchange to a permanent implant with the same safety profile as saline tissue expanders, and consistent with previous trials, demonstrated a high level of satisfaction amongst patients and physicians. The results of this trial were presented at the prestigious American Society of Plastic Surgeon's (ASPS)

meeting. This presentation received the top presentation award for the entire conference.

Pending the receipt of FDA clearance for the AeroForm, we will commence commercial launch in the US later in 2016. The US presents a major opportunity and it is fitting that preparations for launch are well underway. The company has been steadily building awareness amongst key opinion leaders and early adopters through its clinical studies, publications and conference attendance. Additionally, it has commenced the build-out of a high calibre commercial team in the US and the manufacturing transfer – which will deliver benefits in terms of increased capacity and margin improvement – is now underway.

I would like to thank my fellow Board members, including CEO and President Scott Dodson, and the entire AirXpanders team for their tireless dedication and hard work. Through the efforts of Scott and the team, we all look forward to building on the success achieved in 2015 and continuing to grow shareholder value in 2016.

To our shareholders, we are very grateful for your support in our first year as a listed company and we look forward to engaging with you in the year ahead.

Barry Cheskin

Barry Cheskin
Chairman

AirXpanders 2015 Highlights



June 2015

Listed on the Australian Securities Exchange (AXP) following an oversubscribed IPO



July 2015

Full commercial launch of AeroForm commenced in Australia



August 2015

AirXpanders' XPAND pivotal trial meets primary endpoint



October 2015

AirXpanders presents successful XPAND pivotal trial data at ASPS Meeting



December 2015

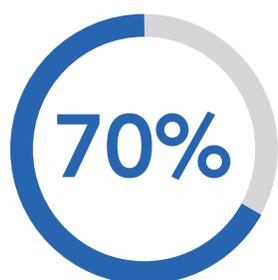
AirXpanders submits de novo application to U.S. FDA for AeroForm



January 2016

AirXpanders reports it has gained almost 20% market share in first six months on market in Australia

CEO's Report



Since launching in Australia, revenue has grown each quarter, increasing by 70% in the December quarter



The 2015 calendar year was a period of strong growth for AirXpanders. This year we successfully listed on the Australian Securities Exchange (ASX), laid the foundation to support the next phase of growth and accelerated our market share in Australia - all while preparing for commercial launch in the United States.

In December 2015, the US Congress passed the Breast Cancer Patient Education Act, and its implications are vast for our company. Currently, less than half of all women requiring a mastectomy are offered breast reconstruction surgery, and fewer than one in five elect to undergo the procedure. The Act now mandates that all breast cancer patients are educated and informed of the availability of breast reconstruction, prostheses, and other options. This represents a significant opportunity for AirXpanders in the US market which alone has an addressable market in the order of US\$800+ million.

Operational Review

Since listing on the ASX on 22 June 2015, AirXpanders has achieved a number of important operational milestones. The highlights include:

- Achieving a 20 per cent market share in the six months following the commercial launch of the AeroForm tissue expander in Australia. This achievement is remarkable for a medical device company and illustrates the strong relationship we have with surgeons as well as

increasing recognition of AeroForm as the tissue expander of choice for breast cancer patients.

- Training approximately 70 Australian surgeons on the use of AeroForm and complete on-boarding of the device at 20 major public and private hospitals in Australia.
- Reporting on the Company's pivotal U.S. XPAND trial, which met its primary endpoint in 150 mastectomy patients, in August 2015. This study helped pave the way for our application to the US Food and Drug Administration (FDA). AirXpanders submitted a de novo application for regulatory approval of the AeroForm device, and pending clearance, will commence the commercial launch of AeroForm in the US in second half of 2016.
- Presenting our XPAND pivotal trial data at the American Society of Plastic Surgeons (ASPS) conference, the world's largest plastic surgery meeting. The XPAND trial showed that 98 percent of patients found the AeroForm device easy to use, and that AeroForm significantly reduced the time to expansion – an average of 21 days for the AeroForm group versus 46 days for the saline group.
- We commenced the transfer of our manufacturing line from our existing centre in California to a certified contract manufacturer in Costa Rica, one of the top seven suppliers of medical devices to the US market. The transfer is expected to be complete in

2016 and will enable AirXpanders to increase its manufacturing capacity from its current 4,000 units per year to over 100,000 units per year with multiple production lines.

- Making a number of key hires that will accelerate the US launch of AeroForm, including Vice President of Sales, Anthony Carnemolla; Senior Director of Global Marketing, Jennie Kim, and Director of Customer Relations, Gary Jones. Each of these individuals possesses significant expertise in their related fields and will be a strong asset to the AirXpanders team.

Financial Position as of 31 December 2015

AirXpanders' total revenue for the year was US\$292,608. Since launching in Australia, revenue has grown each quarter, increasing by 70% in the December quarter.

Overall the company reported a net loss of US\$11.2m with total cash holdings of US\$19.1m.

Our quarterly sales trend has gained traction and continues upwards with revenue increasing 70 percent in the December quarter.

Looking ahead

2015 was a milestone year for AirXpanders, and our highly successful activity in Australia provides us with a

blueprint for future growth, especially as we pursue expansion into the US market. Our major goals for 2016 include:

- Working with the FDA to secure regulatory approval for marketing of AeroForm in the United States;
- Establishing a strong sales force in the US ahead of our commercial launch, planned for the second half of 2016;
- Continuing to accelerate market share in Australia;
- Completing automation and transfer of manufacturing to Costa Rica; and
- Releasing device enhancements including a new dose controller and a further advanced version of the tissue expander.

We are inspired and motivated every day by breast cancer patients undergoing their own personal reconstruction journey, and we are committed to improving these women's experiences via a more efficient and less painful tissue expansion process.

I am excited about the significant short term opportunities ahead for AirXpanders and on behalf of the Board and Management, we greatly appreciate the support of our shareholders.

Scott Dodson
President & CEO



**We are inspired
and motivated
every day by
breast cancer
patients
undergoing their
own personal
reconstruction
journey**





A Patient's Perspective: Rebecca Reidy

“

...I feel incredibly lucky that I was referred to a surgeon who has used AeroForm. There is nothing easy about dealing with cancer, but my reconstruction experience has been positive.

”

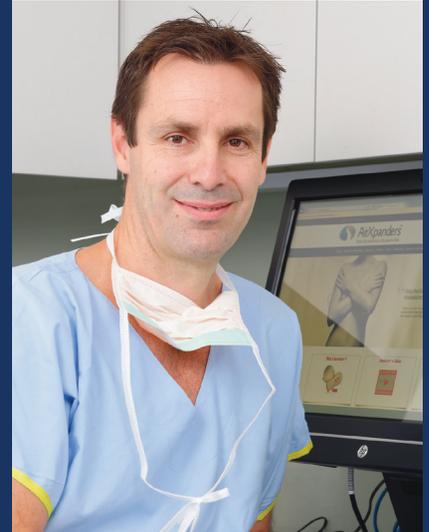
At 43 years of age, following my mother's breast cancer diagnosis and treatment, I had my first mammogram, and within a week was dealing with my own breast cancer diagnosis requiring a right mastectomy. While it was important for me to know the cancer was being removed through the mastectomy, retaining some normalcy to my physical shape was essential to me. My plastic surgeon, Mr Damien Grinsell, recommended AirXpanders and AeroForm tissue expander. It sounded like a good solution, but as I was dealing with a completely new set of circumstances and information at the time, and it is only in hindsight that I realise how lucky I was to be referred to a surgeon who used this product.

Now, eight weeks' post-surgery, I can appreciate the benefits of AeroForm. My new breast shape is better than I could have imagined, and once I recovered from surgery, I experienced no pain. Using the wireless controller to expand the

AeroForm was simple and allowed me to be in control of the breast size I will end up with. I am half way through my chemotherapy treatment and I'm not experiencing breast pain, and I don't need regular doctor's appointments for injections to inflate my tissue expander. Chemotherapy is certainly tough enough without added needles and discomfort. And, four weeks after my final chemotherapy session, I will be ready to complete my reconstruction. No delays means I can get my cancer treatment wrapped up sooner. Like most people in my situation I went into this possessing very little knowledge of my breast reconstruction options. But I have now heard and read many other patients' treatment and reconstruction experiences, I feel incredibly lucky that I was referred to a surgeon who has used AeroForm. There is nothing easy about dealing with cancer, but my reconstruction experience has been positive.

Rebecca Reidy

A Surgeon's Perspective: Mr Damien Grinsell (MBBS, FRACS Plas)



I had been following with interest the progress of the AeroForm tissue expander from the initial development phase, and it was a great opportunity to be one of the first surgeons to use them. I believe this development to be the greatest advancement in tissue expander and breast reconstruction since the introduction of the integrated port expanders.

It has completely changed my practice. In particular, the removal of intermittent needle based inflations has been particularly advantageous

to improving patient anxiety and comfort levels. Similar to being given a PCA (Patient Controlled Analgesia) to control pain, patients embrace being in control of the expansion process and having the ability to temporarily cease expansion at any time if they feel any discomfort. The pure simplicity of the patient controlled expansion is the strength of the device.

**Mr Damien Grinsell
(MBBS, FRACS Plas)**



The pure simplicity
of the patient
controlled
expansion is the
strength of the
device.



AeroForm: The innovative, patient-controlled tissue expander system delivering improved standards of care



Independent Auditor's Report

To the Board of Directors and Stockholders of
AirXpanders, Inc.
Palo Alto, California

Report on the Financial Statements

We have audited the accompanying financial statements of AirXpanders, Inc. (the Company), which comprise the balance sheets as of December 31, 2015 and 2014, and the related statements of operations, stockholder's equity (deficit) and cash flows for the years then ended and the related notes to the financial statements, (collectively, financial statements).

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

To the Board of Directors and Stockholders of
AirXpanders, Inc.
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Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2015 and 2014, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

SingerLewak LLP

SingerLewak LLP

San Jose, California
February 25, 2016

Financial Statements

Balance Sheets

December 31, 2015 and 2014

ASSETS

	2015	2014
Current assets		
Cash and cash equivalents	\$19,112,802	\$1,650,736
Accounts receivable	76,884	-
Inventory	527,020	171,668
Prepaid expenses and other current assets	194,593	47,043
Total current assets	19,911,299	1,869,447
Property and equipment, net	909,662	155,306
Other assets	128,628	113,044
Total assets	\$20,949,589	\$2,137,797

The accompanying notes are an integral part of these financial statements.

LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIT)

	2015	2014
Current liabilities		
Current portion of long-term debt, net of discount	\$1,500,000	\$993,089
Accounts payable	874,396	401,825
Accrued expenses	393,959	195,165
Total current liabilities	2,768,355	1,590,079
Long-term debt, less current portion, net of discount		
Warrant liabilities	-	164,138
Total liabilities	\$3,904,374	\$4,325,174
Commitments (Note 8)		
Stockholders' equity (deficit)		
Convertible preferred stock, par value \$0.001, 0 and 132,356,630 authorized respectively; 0 and 130,509,868 shares issued and outstanding at December 31, 2015 and 2014, respectively	\$-	\$130,510
Preferred stock, par value \$0.001; 10,000,000 and 0 shares authorized respectively; 0 and 0 shares issued and outstanding at December 31, 2015 and 2014, respectively	-	-
Common stock; par value \$0.001, 300,000,000 and 48,596,637 shares authorized at December 31, 2015 and 2014, respectively; 70,427,195 and 901,665 shares issued and outstanding at December 31, 2015 and 2014, respectively	70,426	902
Additional paid-in capital	63,880,186	33,425,263
Accumulated deficit	(46,905,397)	(35,744,052)
Total stockholders' equity (deficit)	17,045,215	(2,187,377)
Total liabilities and stockholders' equity (deficit)	\$20,949,589	\$2,137,797

Statements of Operations

For the Years Ended December 31, 2015 and 2014

	2015	2014
Revenue	\$292,608	\$-
Cost of goods sold	1,378,145	-
Gross loss	(1,085,537)	-
Operating expenses		
Research and development	3,131,118	1,193,930
Clinical trials and regulatory	1,696,231	2,948,742
Selling, general and administrative	5,167,517	2,228,808
Total operating expenses	9,994,866	6,371,480
Operating loss	(11,080,403)	(6,371,480)
Interest expense	421,996	561,075
Other (income) expense, net	(341,054)	45,196
Net loss	\$(11,161,345)	\$(6,977,751)

The accompanying notes are an integral part of these financial statements.

Statements of Stockholders' Equity (Deficit)

For the Years Ended December 31, 2015 and 2014

	Convertible Preferred Stock		Common Stock		Additional Paid-In Capital	Accumulated Deficit	Total Stockholders' Equity (Deficit)
	Issued and Outstanding Shares	Amount	Issued and Outstanding Shares	Amount			
Balance, January 1, 2014	125,509,868	\$125,510	901,665	\$902	\$32,342,921	\$(28,766,301)	\$3,703,032
Additional Series E preferred stock for cash (net of issuance costs of \$20,981)	5,000,000	5,000	-	-	974,019	-	979,019
Stock-based compensation	-	-	-	-	108,323	-	108,323
Net loss	-	-	-	-	-	(6,977,751)	(6,977,751)
Balance, December 31, 2014	130,509,868	\$130,510	901,665	\$902	\$33,425,263	\$(35,744,052)	\$(2,187,377)
Issuance of common stock for cash (net of issuance costs of \$2,872,649)	-	-	25,217,180	25,217	25,055,056	-	25,080,273
Exercise of warrants to purchase common stock	-	-	9,780,489	9,780	39,122	-	48,902
Exercise of Stock Options	-	-	2,965	3	520	-	523
Conversion of convertible bridge notes payable and accrued interest of \$70,233 into common stock	-	-	4,412,474	4,412	5,025,808	-	5,030,220
Conversion of convertible preferred stock into common stock	(130,509,868)	(130,510)	30,112,422	30,112	100,398	-	-
Conversion of warrants to purchase preferred stock into warrants to purchase common stock	-	-	-	-	122,516	-	122,516
Stock-based compensation	-	-	-	-	111,503	-	111,503
Net loss	-	-	-	-	-	(11,161,345)	(11,161,345)
Balance, December 31, 2015	-	\$-	70,427,195	\$70,426	\$63,880,186	\$(46,905,397)	\$17,045,215

Statements of Cash Flows

For the Years Ended December 31, 2015 and 2014

	2015	2014
Cash flows from operating activities		
Net loss	\$(11,161,345)	\$(6,977,751)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	85,619	36,851
Amortization of debt discount	9,060	23,729
Interest on convertible bridge notes payable converted to common stock	70,233	110,356
Change in fair value of warrant liabilities	(41,622)	50,684
Inventory provision	527,444	160,406
Stock-based compensation	111,503	108,323
Changes in operating assets and liabilities		
Accounts receivable	(76,884)	-
Inventory	(882,796)	(332,074)
Prepaid expenses and other assets	(147,550)	6,448
Accounts payable	472,571	(26,689)
Accrued expenses	198,794	48,661
Net cash used in operating activities	(10,834,973)	(6,791,056)
Cash flows from investing activities		
Purchase of property and equipment	(839,975)	(95,874)
Cash used in investing activities	(839,975)	(95,874)

The accompanying notes are an integral part of these financial statements.

Statements of cash flows. For the Years Ended December 31, 2015
and 2014 (Continued)

	2015	2014
Cash flows from financing activities		
Proceeds from convertible bridge notes payable	4,959,987	-
Proceeds from notes payable	-	3,500,000
Principal payments on notes payable	(937,087)	(1,083,148)
Proceeds from issuance of common stock, net of issuance costs	25,080,273	979,019
Proceeds from exercise of stock options	523	-
Proceeds from exercise of warrants for common stock	48,902	-
Debt issue costs	(15,584)	(83,053)
Net cash provided by financing activities	29,137,014	3,312,818
Increase (decrease) in cash and cash equivalents	17,462,066	(3,574,112)
Cash and cash equivalents - beginning of period	1,650,736	5,224,848
Cash and cash equivalents - end of period	\$19,112,802	\$1,650,736
Supplemental disclosure		
Cash paid for interest	\$240,144	\$429,311
Cash paid for taxes	\$800	\$800
Supplemental schedule of noncash investing and financing activities:		
Conversion of preferred stock to common stock in connection with initial public offering	\$34,632,758	\$-
Conversion of convertible bridge notes payable and accrued interest to common stock in connection with initial public offering	\$5,030,220	\$-
Conversion of warrant liabilities to equity	\$122,516	\$-

Notes to Financial Statements

December 31, 2015 and 2014

NOTE 1 – DESCRIPTION OF BUSINESS

AirXpanders, Inc. (“AirXpanders” or the “Company”) is a Delaware corporation formed on March 17, 2005, and is headquartered in Palo Alto, California. The Company has been primarily engaged in developing initial product technology, recruiting personnel and raising capital.

As a medical device company, AirXpanders is focusing in the field of tissue expansion after mastectomy, with an emphasis on breast reconstruction. The Company is designing the novel AeroForm patient controlled tissue expander. The AeroForm system consists of a self-contained expander (which is implanted in a similar manner to traditional saline expanders following a mastectomy), and a small hand-held wireless remote control unit. The lipstick-sized carbon dioxide (CO₂) reservoir in the expander gradually releases a predetermined amount of CO₂ through a small internal valve, eliminating the need for frequent saline injections at doctors’ offices typically associated with current on-market expanders.

NOTE 2 – LIQUIDITY

The accompanying financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the settlement of liabilities and commitments in the normal course of business for the foreseeable future. The Company has incurred net losses from operations since its inception and has an accumulated deficit of \$46,905,397 at December 31, 2015. The Company recorded net losses of \$11,161,345 and \$6,977,751 for the years ended December 31, 2015 and 2014, respectively. The Company also recorded negative cash flows from operating activities for the years ended December 31, 2015 and 2014 of \$10,834,973 and \$6,791,056, respectively. To date, the Company’s product candidates have been approved for marketing and sales in Australia and Europe, the Company started selling its product in Australia in January 2015. Management expects operating losses and cash flow deficits to continue for the foreseeable future. The Company’s ability to achieve profitability is dependent primarily on its ability to successfully gain market share in Australia and Europe, obtain regulatory approvals in the U.S. by the U.S. Food and Drug Administration (FDA) and gain market share in the U.S. The regulatory approval process is expensive, time-consuming, and uncertain, and any denial or delay of approval could have a material adverse effect on the Company. The accompanying financial statements do not include any adjustments that may be needed if the Company were unable to continue as a going concern.

In June 2015, the Company issued 29,629,654 shares of common stock in connection with an initial public offering (“IPO”) on the Australian Securities Exchange (ASX). The Company raised a total of \$30,089,162, net of issuance costs of \$2,872,649. Of this amount, \$28,001,824 (AU\$36.5 million) were proceeds directly from the IPO; \$4,959,987 were proceeds from the private placement of convertible bridge notes payable. In January 2014, the Company borrowed \$3,500,000 under a loan and security agreement with a financial institution which expires in July 2017. The Company had the option to borrow an additional \$3,500,000 under the agreement, with the same terms, if certain conditions were met. This option expired in June 2015 and the Company did not borrow the additional \$3,500,000.

NOTE 3 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (US GAAP).

Use of Estimates

The preparation of financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of expenses during the reporting period. Actual results could differ materially from those estimates. The Company's most significant estimates relate to the valuation of its common stock prior to the IPO, options and warrant liabilities and valuation of its inventory at lower of cost or market.

Certain Significant Risks and Uncertainties

The Company operates in a dynamic, highly competitive industry and believes that changes in any of the following areas could have a material adverse effect on the Company's future financial position, results of operations, or cash flows; ability to obtain future financing; advances and trends in new technologies and industry standards; regulatory approval and market acceptance of the Company's products; development of sales channels; certain strategic relationships; litigation or claims against the Company based on intellectual property, patent, product, regulatory, or other factors; and the Company's ability to attract and retain employees necessary to support its growth.

Concentrations of Credit Risk

Financial instruments that potentially subject the Company to credit risk consist primarily of cash and cash equivalents. The Company maintains all of its U.S. cash balances at one financial institution, which at times may exceed the Federal Deposit Insurance Corporation (FDIC) limits of \$250,000 for interest-bearing accounts. At December 31, 2015 and 2014, the Company had cash balances of approximately \$16,508,489 and \$1,425,736 that were in excess of the FDIC limits. The Company also maintains all of its Australian cash balance at one financial institution, which at times may exceed the Australian government guaranteed limit of \$182,188 (AU\$ 250,000). At December 31, 2015, the Company had a cash balance of approximately \$2,197,125 that was in excess of the guaranteed limit.

Cash and Cash Equivalents

The Company considers all highly liquid investments with an original maturity of three months or less to be cash equivalents. At December 31, 2015, the Company maintained a balance of \$16,758,489 with one U.S. financial institution and the equivalent of approximately U.S. \$2,379,313 with one Australian financial institution. Restricted cash of \$25,000 at December 31, 2015 and 2014, which serves as collateral for corporate credit cards, is included in other assets in the balance sheet.

Inventory

Inventory is valued at the lower of cost or market value, with cost determined by the first-in, first-out method.

Property and Equipment

Property and equipment are stated at cost, net of accumulated depreciation. Depreciation is computed using the straight-line method over the estimated useful lives of the assets, generally three to five years. Leasehold improvements and property and equipment under capital leases are depreciated over the shorter of the estimated useful lives of the assets or the lease terms.

Expenditures for repairs and maintenance are charged to expense as incurred. Upon disposition of an asset, the cost and related accumulated depreciation are removed from the accounts and the resulting gain or loss is reflected in the statement of operations.

Impairment of Long-Lived Assets

The Company's long-lived assets and other assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the asset may not be recoverable. Recoverability of an asset to be held and used is measured by a comparison of the carrying amount of an asset to the future undiscounted cash flows expected to be generated by the asset. If such asset is considered to be impaired, the impairment to be recognized is measured as the amount by which the carrying amount of the asset exceeds its fair value. Through December 31, 2015, the Company had not experienced impairment losses on its long-lived assets.

Fair Value of Financial Instruments

The Company follows Financial Accounting Standards Board ("FASB") Accounting Standards Codification Topic No. 820, *Fair Value Measurement* ("ASC 820"), which clarifies fair value as an exit price, establishes a hierarchal disclosure framework for measuring fair value, and requires extended disclosures about fair value measurements. The provisions of ASC 820 apply to all financial assets and liabilities measured at fair value.

As defined in ASC 820, fair value represents the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. As a result, fair value is a market-based approach that should be determined based on assumptions that market participants would use in pricing an asset or a liability. As a basis for considering these assumptions, ASC 820 defines a three-tier value hierarchy that prioritizes the inputs used in the valuation methodologies in measuring fair value.

- Level 1 – Quoted prices in active markets for identical assets or liabilities.
- Level 2 – Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
- Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

The fair value hierarchy also requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

The following table sets forth by level, within the fair value hierarchy, the Company's assets measured at fair value in the balance sheet as of December 31, 2015:

	Level 1	Level 2	Level 3	Total
Cash and cash equivalents	\$19,112,802	\$-	\$-	\$19,112,802
Total assets at fair value	\$19,112,802	\$-	\$-	\$19,112,802

The following table sets forth by level, within the fair value hierarchy, the Company's assets and liabilities measured at fair value in the balance sheet as of December 31, 2014:

	Level 1	Level 2	Level 3	Total
Cash and cash equivalents	\$1,650,736	\$-	\$-	\$1,650,736
Total assets at fair value	\$1,650,736	\$-	\$-	\$1,650,736
Warrant liabilities	\$-	\$-	\$164,138	\$164,138
Total liabilities at fair value	\$-	\$-	\$164,138	\$164,138

See Note 11 for discussion of the valuation methodology and inputs for the warrant liabilities.

At December 31, 2015 and 2014, the Company had the following financial instruments for which disclosure only of fair value is required:

Long-term debt – Valued at carrying value which is considered to be representative of its fair value based on current market rates available to the Company for comparable borrowing facilities.

Revenue Recognition

The Company recognizes revenue from sales of its products in accordance with the Revenue Recognition Topic ASC 605. The Company recognizes revenue from product sales upon delivery, provided there are no uncertainties regarding customer acceptance, there is persuasive evidence of an arrangement, the fee is fixed or determinable, and collectability of the related receivable is reasonably assured. This generally occurs after a device has been implanted in a patient.

Accounts Receivable and Allowance for Doubtful Accounts

Accounts receivable are stated at cost, net of allowance for doubtful accounts. Credit is extended to customers based on an evaluation of their financial condition and other factors. The Company generally does not require collateral or other security to support accounts receivable. The Company performs ongoing credit evaluations of its customers and maintains an allowance for doubtful accounts.

The Company estimates its allowance for doubtful accounts by evaluating specific accounts where information indicates that customers may have an inability to meet their financial obligations and receivable amounts are outstanding for an extended period beyond the invoice terms. In these cases, the Company uses assumptions and judgment, based on the best available facts and circumstances, to either record a specific allowance against these customer balances or to write the balances off. The accounts receivable aging is reviewed on a regular basis and write-offs are recorded on a case-by-case basis net of any amounts that may be collected. Allowance charges are recorded as operating expenses. The Company did not have an allowance for doubtful accounts at December 31, 2015.

Concentration

24% of the Company's revenue for the year ended December 31, 2015 was from one customer and two customers accounted for 47% of the accounts receivable balance at December 31, 2015.

Reverse Stock Split

In May 2015 the Company's shareholders approved a 5-for-1 reverse stock split of all outstanding common stock and all securities exercisable into common stock. All amounts for common stock, preferred stock conversion ratios, stock options and warrants in the financial statements have been retroactively adjusted to reflect the effect of the reverse stock split.

Stock-Based Compensation

Stock-based compensation is measured at the grant date based on the fair value of the award. The fair value of the award that is ultimately expected to vest is recognized as expense on a straight-line basis over the requisite service period, which is generally the vesting period. The expense recognized for the portion of the award that is expected to vest has been reduced by an estimated forfeiture rate. The forfeiture rate is determined at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates.

The Company uses the Black-Scholes option-pricing model (the "Black-Scholes model") as the method for determining the estimated fair value of stock options.

Expected Term

The Company's expected term represents the period that the Company's stock-based awards are expected to be outstanding and is determined using the simplified method, which essentially equates to a weighted average of the vesting periods and total term of the award.

Expected Volatility

Expected volatility is estimated using comparable public companies volatility for similar terms.

Expected Dividend

The Black-Scholes model calls for a single expected dividend yield as an input. The Company has never paid dividends and has no current plans to pay dividends on its common stock.

Risk-Free Interest Rate

The risk-free interest rate used in the Black-Scholes model is based on the U.S. Treasury zero coupon issues in effect at the time of grant for periods corresponding with the expected term of the option.

The Company recognizes the fair value of stock options granted to nonemployees as stock-based compensation expense over the period in which the related services are received.

Research and Development

Costs incurred in research and development activities (including clinical trials) are expensed as incurred. Research and development costs include, but are not limited to, payroll and personnel expenses, laboratory supplies, consulting costs, travel, parts and materials, equipment expenses, and equipment depreciation.

Income Taxes

The Company accounts for income taxes using the asset and liability method. Under this method, deferred income tax assets and liabilities are recorded based on the estimated future tax effects of differences between the financial statement and income tax basis of assets and liabilities. In addition, deferred tax assets are recorded for the future benefit of utilizing net operating loss and tax credit carryovers. Deferred tax assets and liabilities are measured using the enacted tax rates applied to taxable income. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. A valuation allowance is provided against the Company's deferred income tax assets when it is more likely than not that the asset will not be realized.

Significant judgment is required in determining any valuation allowance recorded against deferred tax assets. In assessing the need for a valuation allowance, the Company considers all available evidence, including past operating results, estimates of future taxable income and the feasibility of tax planning strategies. In the event that the Company changes its determination as to the amount of deferred tax assets that are more likely than not to be realized, the Company will adjust its valuation allowance with a corresponding impact to the provision for income taxes in the period in which such determination is made.

The Company follows authoritative guidance regarding uncertain tax positions. This guidance requires that realization of an uncertain income tax position must be more likely than not (i.e. greater than 50% likelihood of receiving a benefit) before it can be recognized in the financial statements. The guidance further prescribes the benefit to be realized assumes a review by tax authorities having all relevant information and applying current conventions. The interpretation also clarifies the financial statement classification of tax related penalties and interest and sets forth disclosures regarding unrecognized tax benefits. The Company recognizes potential accrued interest and penalties related to unrecognized tax benefits as income tax expense.

Development-Stage Company, Early adoption of ASU 2014-10

The Company was previously classified as a development-stage company as defined in Accounting Standards Codification (“ASC”) No. 915, Development Stage Entities. The Company has elected to early adopt Accounting Standards Update (“ASU”) 2014-10 (“ASU 2014-10”), which eliminates the additional disclosures previously required for development stage companies, in particular, the inception-to-date reporting for the statement of operations, statement of cash flows, and statement of stockholders’ equity (deficit).

Recent Accounting Pronouncements

In November, 2015, the FASB issued ASU 2015-17, “Income Taxes”. The new guidance requires that all deferred tax assets and liabilities, along with any related valuation allowance for each tax-paying jurisdiction within each tax-paying component, be classified as noncurrent on the balance sheet. The new guidance will be effective for public business entities in fiscal years beginning after December 15, 2016, including interim periods within those years. Early adoption is permitted for all entities as of the beginning of an interim or annual reporting period. The Company does not expect this guidance to have significant impact on its financial statements.

In July 2015, the FASB issued ASU 2015-11, “Inventory (Topic 330): Simplifying the Measurement of Inventory”. ASU 2015-11 more closely aligns the measurement of inventory in U.S. GAAP with the measurement of inventory in International Financial Reporting Standards by requiring companies using any methods of inventory valuation other than last-in, first-out or the retail inventory methods to measure inventory using the lower of cost and net realizable value, where net realizable value is the estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. For public business entities, ASU 2015-11 is effective for annual reporting periods beginning after December 15, 2016 including interim periods within those fiscal years. ASU 2015-11 should be applied prospectively with earlier application permitted as of the beginning of an interim or annual reporting period. The Company is currently evaluating the impact of this ASU on its financial statements.

In May 2014, the FASB issued ASU No. 2014-09, “Revenue from Contracts with Customers (Topic 606)”. The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. To achieve that core principle, an entity should 1) identify the contract(s) with a customer, 2) identify the performance obligations in the contract, 3) determine the transaction price, 4) allocate the transaction price to the performance obligations in the contract, and 5) recognize revenue when (or as) the entity satisfies a performance obligation. In July 2015, the FASB deferred for one year the effective date of the new revenue standard, but early adoption will be permitted. The new standard will be effective for the Company on January 1, 2018. The Company is currently evaluating the impact of this ASU on its financial statements.

In April 2015, the FASB issued ASU No. 2015-03, “Interest – Imputation of Interest (Topic 835): Simplifying the Presentation of Debt Issuance Costs”. This ASU simplifies the accounting for debt issuance costs by requiring such costs to be presented as a direct deduction from the related debt liability rather than as an asset. Debt disclosures will include the face amount of the debt liability and the effective interest rate.

The ASU requires retrospective application and represents a change in accounting principle. The update is effective for fiscal years beginning after December 15, 2015. Early adoption is permitted for financial statements that have not been previously issued. The Company is currently evaluating the impact of this ASU on its financial statements.

In August 2014, the FASB issued ASU No. 2014-15, "Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern" which requires that management of public and private companies (rather than the independent auditor) to evaluate and disclose whether there are conditions and events that raise substantial doubt about the entity's ability to continue as a going concern within one year after the financial statements are issued (or available to be issued.) Management will be required to make this evaluation for both annual and interim reporting periods, if applicable. Management also is required to evaluate and disclose whether its plans alleviate that doubt. The new standard is effective for annual periods ending after 15 December 2016 and for annual and interim periods thereafter. Early adoption is permitted for annual or interim reporting periods for which the financial statements have not previously been issued. The Company is currently evaluating the impact of this ASU on its financial statements.

NOTE 4 – INVENTORY

Inventory consisted of the following at December 31, 2015:

	2015	2014
Raw materials	\$211,169	\$37,258
Work in progress	241,949	16,052
Finished goods	64,404	118,358
Inventory in transit	9,498	-
Inventory	\$527,020	\$171,668

The Company had written down its inventory to market value by \$687,850 and \$160,406 for the years ended December 31, 2015 and 2014 respectively.

NOTE 5 – PROPERTY AND EQUIPMENT

Property and equipment consists of the following at December 31:

	2015	2014
Machinery and equipment	\$714,382	\$433,682
Computer equipment	121,926	74,716
Furniture and fixtures	77,457	72,060
Leasehold improvements	100,354	36,875
Software licenses	19,061	19,061
Office equipment	8,679	1,878
Construction in progress	395,903	-
Property and equipment, gross	1,437,762	638,272
Accumulated depreciation and amortization	(528,100)	(482,966)
Property and equipment, net	\$909,662	\$155,306

Depreciation and amortization expense amounted to \$85,619 and \$36,851 for the years ended December 31, 2015 and 2014, respectively.

NOTE 6 – ACCRUED EXPENSES

Accrued expenses consisted of the following at December 31:

	2015	2014
Accrued payroll and related expenses	\$199,290	\$92,760
Accrued rent payable	28,976	4,579
Accrued other	165,693	97,826
Total accrued expenses	\$393,959	\$195,165

NOTE 7 – DEBT FINANCING

In March 2011, the Company borrowed \$3,000,000 under a loan and security agreement with a financial institution which expired in September 2014. In January 2014, the Company repaid the entire loan balance. Interest was paid monthly on the principal amount at 9.01%. Under the terms of the agreement, interest-only payments were made monthly through September 2011, with principal payments commencing in October 2011, due in 36 equal monthly installments. A fee of \$165,000 was due at maturity. The Company could prepay the entire loan amount by providing a written ten day notice prior to such prepayment and pay all outstanding principal, interest and prepayment fee plus any default fees and all other sums that shall have become due and payable. The loan was secured by substantially all of the Company's assets, excluding intellectual property.

In connection with this loan agreement, the Company granted a warrant to the financial institution to purchase 96,000 shares of Series C convertible preferred stock ("Series C") at \$1.25 per share. The warrant is exercisable at the option of the holder at any time through February 28, 2021 and is outstanding at December 31, 2015 (see Note 11). As a result of the Company's initial public offering in June 2015 and conversion of all outstanding preferred stock into common stock, the warrants were converted into warrants for 120,000 shares of common stock at an exercise price of \$1.25 per share. The fair value of the warrant of \$76,647 on the date of issuance was recorded as a debt discount. The debt discount was being amortized over the expected term of the loan as a component of interest expense. The Company recorded \$0 and \$31,921 to interest expense related to amortization of this debt discount for the years ended December 31, 2015 and 2014, respectively.

In January 2013, the Company entered into a loan modification agreement related to the loan and security agreement, to make monthly repayments of interest only from February 1, 2013 to June 1, 2013. The Company paid a modification fee of \$15,000. In conjunction with the modification, the Company issued a warrant for the purchase of 29,629 shares of Series D Preferred Stock at an exercise price of \$1.35. As a result of the Series E round of financing during 2013, the holder of the warrant had the election under their existing warrant agreement to convert their warrants into warrants for 40,000 shares of Series E at an exercise price of \$1.00 per share. As a result of the Company's initial public offering in June 2015 and conversion of all outstanding preferred stock into common stock, the warrants were converted into warrants for 40,000 shares of common stock at an exercise price of \$1.00 per share. This warrant is outstanding at December 31, 2015 (see Note 11).

In January 2014, the Company borrowed \$3,500,000 under a loan and security agreement with a financial institution which expires in July 2017. Interest is paid monthly on the principal amount at 7.34%. The loan is secured by substantially all of the Company's assets, excluding intellectual property. Under the terms of the agreement, interest-only payments were made monthly through March 2015, with principal payments commencing in April 2015, due in 28 equal monthly installments. A fee of \$271,250 is due at maturity, which is being accrued over the term of the loan. The Company can prepay the entire loan amount by providing a written five day notice prior to such prepayment and pay all outstanding principal, interest and prepayment fees plus any default fees and all other sums that shall have become due and payable.

Part of the loan proceeds were used to pay off the balance of the loan borrowed in March 2011.

In March 2015, the Company amended the loan and security agreement to extend the interest-only period from March 2015 to April 2015, with principal payments commencing in May 2015, due in 27 equal monthly installments. The Company had the option to borrow an additional \$3,500,000 under the agreement, with the same terms, if certain conditions were met. This option expired unexercised in June 2015. The credit agreement includes a covenant whereby the Company is required to maintain all of the funds owned by it in the continental United States, provided that the Company may hold funds with an aggregate value of less than \$1,000,000 (or the foreign currency equivalent thereof) outside of the United States. At December 31, 2015, the Company had approximately \$2,379,313 of funds held outside of the United States which was in excess of the allowed limit per the covenant. In November 2015, the lender signed a waiver stating that despite the covenant violation, it would allow a grace period ending May 15, 2016 to comply with this covenant. Until that date, the loan may not be called. The Company plans to cure the covenant violation during the grace period and as a result has not classified all of this debt as current in the balance sheet.

In connection with the loan agreement, the Company granted a warrant to the financial institution for the purchase of 52,500 shares of Series E convertible preferred stock ("Series E") at \$1.00 per share. The warrant is exercisable at the option of the holder at any time through January 15, 2024. As a result of the Company's initial public offering in June 2015 and conversion of all outstanding preferred stock into common stock, the warrants were converted into warrants for 52,500 shares of common stock at an exercise price of \$1.00 per share. The fair value of the warrant of \$31,710 on the date of issuance was recorded as a debt discount. The Company recorded \$9,060 and \$8,683 to interest expense related to amortization of this debt discount for the years ended December 31, 2015 and 2014 respectively. As of December 31, 2015, the unamortized discount on the debt is \$13,967. This warrant is outstanding at December 31, 2015 (see Note 11).

The Company recorded \$346,251 and \$561,075 of interest expense on the loans for the years ended December 31, 2015 and 2014, respectively. At December 31, 2015, \$2,636,019 was outstanding under this loan agreement.

In February and June 2015, the Company raised through a private placement of convertible bridge notes payable a total of \$4,959,987 in cash proceeds. The convertible bridge notes payable carried interest at 7% per annum. All the convertible bridge notes payable and accrued interest of \$70,233 were converted into 4,412,474 shares of common stock as part of Company's initial public offering in June 2015.

At December 31, 2015, future scheduled principal payments are as follows:

For the Years Ending December 31,	
2016	\$1,500,000
2017	1,149,986
Unamortized discount	(13,967)
Total debt	2,636,019
Less current portion	1,500,000
Total noncurrent portion of debt	\$1,136,019

NOTE 8 – COMMITMENTS

Lease Obligations

The Company leases its office space under a non-cancelable operating lease. Monthly base rent payments range from \$12,807 to \$21,627. The Company amended the lease to extend the term of the lease from August 2013 through July 2016. In July 2015 the Company signed an agreement to extend its current office space lease to September 30, 2019. Under the same lease agreement, the Company expanded the premises and leased additional office space totaling approximately 5,692 square foot space commencing October 1, 2015.

The Company recognizes rent expense on a straight-line basis over the term of the lease. Rent expense (including common area maintenance) related to the Company's operating leases was \$272,967 and \$203,130 for the years ended December 31, 2015 and 2014, respectively. Deferred rent balance was \$28,976 and \$4,579 at December 31, 2015 and 2014, respectively.

At December 31, 2015 the future rental commitments due under the lease are:

Years Ending December 31,	
2016	347,045
2017	401,842
2018	413,898
2019	317,356
Total	\$1,480,141

Indemnifications

The Company has agreed to indemnify its officers and directors for certain events or occurrences arising as a result of the officers or directors serving in such capacity. The Company has a directors and officers' liability insurance policy that limits its exposure and enables the Company to recover a portion of any future amounts paid resulting from the indemnification of its officers and directors. In addition, the Company enters into indemnification agreements with other parties in the ordinary course of business. The Company has not incurred material costs to defend lawsuits or settle claims related to these indemnification agreements. The Company's management believes the estimated fair value of these indemnification agreements is minimal and has not recorded a liability for these agreements as of December 31, 2015 and 2014.

Royalties

The Company uses AeroForm® technology in the products it is developing. AeroForm® embodies inventions that have been patented in certain key jurisdictions. Certain of those patents are held by Shalon Ventures (either alone or jointly with AirXpanders). Shalon Ventures and AirXpanders have entered into a License Agreement dated March 9, 2005 (as amended on March 9, 2009 and January 9, 2012) in relation to those inventions (Shalon Ventures License Agreement). Pursuant to the Shalon Ventures License Agreement, Shalon Ventures granted AirXpanders an exclusive license to develop, make, have made, use, offer for sale, sell, have sold, import and export products that, but for the license, would infringe one or more claims of the patents. The license covers all human uses of self-expanding tissue expanders anywhere in the world and includes the right to sublicense.

In consideration for the license, AirXpanders pays Shalon Ventures a running royalty of 3% of net sales of the licensed invention. If the amount of royalties paid in a calendar year is less than \$10,000, then AirXpanders shall also pay Shalon Ventures' out of pocket costs for prosecuting and maintaining the relevant patents. Each party indemnifies the other for any liability arising out of its material breach of the license, or its gross negligence, intentional misconduct and illegal actions. AirXpanders also indemnifies Shalon Ventures for any liability arising out of the commercialization of products using the license. Through December 31, 2015, the Company has incurred \$6,483 in royalty fees.

Mr. Teddy Shalon and Mr. Barry Cheskin are directors and shareholders of the Company. Mr. Cheskin is also the co-founder and chairman of the board of the Company. Mr. Shalon is the Chief Executive Officer and sole shareholder of Shalon Ventures. Mr. Shalon and Mr. Cheskin are each party to an agreement with Shalon Ventures, under which Shalon Ventures has agreed to pay Mr. Shalon 58%, and Mr. Cheskin 8%, of any royalties due to Shalon Ventures from AirXpanders under the Shalon Ventures License Agreement.

NOTE 9 – COMMON STOCK

In May 2015, the Company's shareholders approved a 5-for-1 reverse stock split of all outstanding common stock and all securities exercisable into common stock.

The Company's Articles of Incorporation, as amended, authorize the Company to issue 300,000,000 shares of \$0.001 par value common stock consisting of 200,000,000 shares of common stock Class A and 100,000,000 shares of common stock Class B. Class A common stockholders are entitled to dividends when and if declared by the Board of Directors, Class B common stockholders are not entitled to any dividends. The holder of each share of Class A common stock is entitled to one vote and holders of Class B common stock are not entitled to vote. At December 31, 2015 and 2014, no dividends had been declared for common stock. At December 31, 2015 70,427,195 and 0 shares of common stock Class A and Class B respectively were issued and outstanding.

At December 31, 2015 and 2014, common stock that the Company had reserved for issuance was as follows:

	2015	2014
Convertible preferred shares	-	26,101,974
Warrants for common and convertible preferred shares	386,814	10,250,452
Stock option plans	5,590,619	5,362,531
Total	5,977,433	41,714,957

In June 2015, the Company issued 29,629,654 shares of common stock in connection with an IPO on the ASX and conversion of convertible bridge notes payable and related accrued interest. The Company raised a total of \$30,089,162, net of issuance costs of \$2,872,649. Of this amount \$28,001,824 (AU\$36.5 million) were proceeds directly from the IPO; \$4,959,987 were proceeds from the private placement of convertible bridge notes payable.

NOTE 10 – CONVERTIBLE PREFERRED STOCK

The Company's convertible preferred stock consisted of the following at December 31, 2014:

Series E, 8% convertible noncumulative preferred stock, par value \$0.001; 0 and 50,200,000 shares authorized respectively; 0 and 49,499,028 shares issued and outstanding at December 31, 2015 and 2014, respectively (liquidation preference of \$0 and \$9,899,806)	\$49,499
Series D, 8% convertible noncumulative preferred stock, par value \$0.001; 0 and 42,176,625 shares authorized and outstanding at December 31, 2015 and 2014, respectively (liquidation preference of \$0 and \$11,387,689)	42,177
Series C, 8% convertible noncumulative preferred stock, par value \$0.001; 0 and 22,725,718 shares authorized respectively; 0 and 22,245,718 shares issued and outstanding at December 31, 2015 and 2014, respectively (liquidation preference of \$0 and \$5,561,430 respectively)	22,246
Series B-1, 8% convertible noncumulative preferred stock, par value \$0.001; 0 and 9,554,375 shares authorized and outstanding at December 31, 2015 and 2014, respectively (liquidation preference of \$0 and \$4,549,793 respectively)	9,554

Series B, 8% convertible noncumulative preferred stock, par value \$0.001; 0 and 3,375,954 shares authorized respectively; 0 and 3,125,954 shares issued and outstanding at December 31, 2015 and 2014, respectively (liquidation preference of \$0 and \$1,488,579 respectively)	3,126
Series A, 8% convertible noncumulative preferred stock, par value \$0.001; 0 and 4,323,958 shares authorized respectively; 0 and 3,908,168 shares issued and outstanding at December 31, 2015 and 2014, respectively (liquidation preference of \$0 and \$1,861,070 respectively)	3,908
	\$130,510

The Company issued Series A, B, B-1, C, D and E convertible preferred stock during the period from 2005 through 2014, raising a total of \$30,393,627 in cash, net of issuance costs of \$595,493.

As part of Company's initial public offering in June 2015, all outstanding convertible preferred stock was converted into common stock. Series A, B, B-1 and E convertible preferred stock were converted to common stock at a 1:1 ratio, Series C convertible preferred stock was converted to common at a 1.25:1 ratio and Series D convertible preferred stock was converted to common at a 1.35:1 ratio. After conversion of all preferred stock to common stock, the Company cancelled all existing series of preferred stock.

The Company's Articles of Incorporation, as amended, authorize the Company to issue 10,000,000 authorized shares of preferred stock, with rights and privileges for preferred stock to be determined by Company's Board of Directors before issuing preferred shares. At December 31, 2015, the Company has 10,000,000 authorized shares of preferred stock and there are no outstanding shares.

NOTE 11 – STOCK WARRANTS

The Company accounts for warrants in accordance with ASC 480, "*Distinguishing Liabilities from Equity*" ("ASC 480"). Under ASC 480, warrants containing certain features, such as put rights and anti-dilution protection, are required to be accounted for as liabilities and recorded at fair value, with changes in fair value being recorded in the statement of operations. The Company's preferred stock warrants contain such features, requiring liability accounting.

As part of Company's initial public offering in June 2015, all outstanding preferred stock warrants were converted into warrants for common stock. As a result of this conversion the warrants liabilities for \$122,516 were reclassified to additional paid in capital.

The Company is required to reserve authorized but unissued shares of its common and preferred stock in an amount equal to the number of warrant shares purchasable under the arrangements described below.

The Company's warrant liabilities account consisted of the following at December 31:

Date Issued	2015	2014
2007	\$-	\$1,003
2008	-	321
2009	-	59,751
2011	-	47,998
2013	-	23,355
2014	-	31,710
	\$-	\$164,138

The warrant liabilities are revalued at the end of each reporting period with the changes in fair value recorded in other income and expense in the statements of operations. The changes in fair value of these warrants recorded as other income (expense) are as follows for the years ended December 31:

Date Issued	2015	2014
2007	\$(979)	(959)
2008	(313)	(307)
2009	(59,665)	(23,737)
2011	16,372	(23,591)
2013	1,281	(2,090)
2014	1,681	-
	\$(41,623)	\$(50,684)

The fair value of the warrant liabilities was estimated using Black-Scholes model using the following assumptions for 2015 at the date of conversion and December 31, 2014:

	2015	2014
Stock price	\$1.16	\$0.10 - \$0.29
Expected term (years)	0.62 – 8.67 years	1.00 – 9.04 years
Volatility	33.06 – 43.08%	32.20 – 44.70%
Risk-free interest rate	0.24 – 1.99%	0.11 – 2.57%
Dividend yield	- %	- %

In August 2007, in connection with a loan and security agreement, the Company issued a warrant to a financial institution to purchase 62,998 Series A convertible preferred shares at \$2.40 per share. As a result of the Company's initial public offering in June 2015 and conversion of all outstanding preferred stock into common stock, the warrants were converted into warrants for 62,998 shares of common stock at an exercise price of \$2.381 per share. The warrant is exercisable at any time at the option of the holder and expired in 2015.

In March 2008, in connection with a loan and security agreement, the Company issued a warrant to a financial institution to purchase 20,158 Series A convertible preferred shares at \$2.40 per share. As a result of the Company's initial public offering in June 2015 and conversion of all outstanding preferred stock into common stock, the warrants were converted into warrants for 20,158 shares of common stock at an exercise price of \$2.381 per share. The warrant is exercisable at any time at the option of the holder and expired in 2015.

In March 2009, in connection with a loan and security agreement, the Company issued a warrant to a financial institution to purchase 50,000 Series B convertible preferred shares at \$2.40 per share. As a result of the Company's initial public offering in June 2015 and conversion of all outstanding preferred stock into common stock, the warrants were converted into warrants for 50,000 shares of common stock at an exercise price of \$2.381 per share. The warrant is exercisable at any time at the option of the holder and expires in 2016. This warrant remains outstanding at December 31, 2015 and is classified as equity.

In February 2011, in connection with the loan and security agreement, the Company issued a warrant to a financial institution to purchase 96,000 Series C convertible preferred shares at \$1.25 per share (See Note 7). As a result of the Company's initial public offering in June 2015 and conversion of all outstanding preferred stock into common stock, the warrants were converted into warrants for 120,000 shares of

common stock at an exercise price of \$1.25 per share. This warrant remains outstanding at December 31, 2015 and is classified as equity.

In January 2013, in connection with a loan modification agreement entered into with a lender the Company issued a warrant for the purchase of 29,629 shares of Series D Preferred Stock at an exercise price of \$1.35. As a result of the Series E round of financing during 2014, the holder of the warrant had the election under their existing warrant agreement to convert their warrant into a warrant for 40,000 shares of Series E at an exercise price of \$1.00 per share. As a result of the Company's initial public offering in June 2015 and conversion of all outstanding preferred stock into common stock, the warrants were converted into warrants for 40,000 shares of common stock at an exercise price of \$1.00 per share. This warrant remains outstanding at December 31, 2015 and is classified as equity.

In 2013, in connection with the issuance of Series E Preferred Stock the Company issued warrants to Series E investors to purchase 8,904,805 common stock shares at \$0.005 per share. These warrants were exercised during the year ended December 31, 2015.

In January 2014, in connection with the loan and security agreement, the Company issued a warrant to a financial institution to purchase 52,500 Series E convertible preferred shares at \$1.00 per share (See Note 7). As a result of the Company's initial public offering in June 2015 and conversion of all outstanding preferred stock into common stock, the warrants were converted into warrants for 52,500 shares of common stock at an exercise price of \$1.00 per share. This warrant remains outstanding at December 31, 2015 and is classified as equity.

In 2014, in connection with the issuance of Series E Preferred Stock the Company issued warrants to Series E investors to purchase 1,000,000 common stock shares at \$0.005 per share. These warrants were exercised during the year ended December 31, 2015.

NOTE 12 – STOCK-BASED COMPENSATION

In March 2005, the Company adopted the 2005 Equity Incentive Plan (the "2005 Plan"). In May 2015 the Company adopted the 2015 Equity Incentive Plan (the "2015 Plan") collectively, (the "Plans"). The Plans provide for the granting of stock options to employees and consultants of the Company. Options granted under the Plan may be either incentive stock options or nonqualified stock options. Incentive stock options (ISO) may be granted only to Company employees (including officers and directors who are also employees). Nonqualified stock options (NSO) may be granted to Company employees and consultants.

In May 2013, the 2005 Plan was amended to increase the number of shares reserved for issuance under the Plan to 6,170,159 shares of common stock. During the year ended December 31, 2015, the 2005 Plan expired and no future options can be granted under the 2005 Plan.

The Company has reserved 1,500,000 shares under the 2015 Plan in addition a total of 4,099,835 shares reserved under the 2005 Plan will be added to 2015 plan if and when the underlying options are cancelled.

Options under the Plans may be granted for periods of up to 10 years and at prices no less than 100% of the estimated fair value of the shares on the date of grant. In the case of an Incentive Stock Option granted to a holder who, at the time the Option is granted, owns stock representing more than 10% of the voting power of all classes of stock of the Company, the term of the Option shall be up to 5 years from the date of grant and at no less than 110% of the estimated fair value of the shares on the date of grant. Options granted generally vest 1/4 on the 12-month anniversary of the vesting commencement date and 1/48 on each monthly anniversary thereafter.

At December 31, 2015 and 2014, 4,127,900 and 3,786,339 options were vested and expected to vest with a weighted-average exercise price of \$0.3329 and \$0.2850 and weighted average remaining contractual life of 6.56 and 7.33 years, respectively.

The weighted average grant date fair value per share of options granted the years ended December 31, 2015 and 2014 was \$0.3439 and \$0.05 respectively. The fair value of shares vested during the years ended December 31, 2015 and 2014 was \$96,344 and \$149,804 respectively. The weighted average exercise price of options exercised during the year ended December 31, 2015 was \$0.18. There were no options exercised for the year ended December 31, 2014. The intrinsic value of the options exercised during the year ended December 31, 2015 was \$5,343.

In connection with the grant of stock options to employees and non-employees, the Company recorded stock compensation expense to general and administrative expenses in the amounts of \$111,503 and \$108,323 for the years ended December 31, 2015 and 2014, respectively. As of December 31, 2015, unrecognized compensation expense related to employees totaled \$193,737 and will be recognized over approximately 2.40 years.

Activity under the Plan is set forth below:

	Options Available for Grant	Number of Options Outstanding	Exercise Price per Share	Weighted Average Remaining Contractual Life in Years
Balance – December 31, 2013	1,551,925	3,810,607	\$0.30	8.29
Additional shares reserved	-	-	\$-	-
Options granted	(52,026)	52,026	\$0.10	-
Options exercised	-	-	\$-	-
Options forfeited/cancelled	16,924	(16,924)	\$0.20	-
Balance – December 31, 2014	1,516,823	3,845,709	\$0.30	7.33
Additional shares reserved (net of released)	231,052	-	\$-	-
Options granted	(357,127)	357,127	\$0.90	-
Options exercised	-	(2,965)	\$0.18	-
Options forfeited/cancelled	28,579	(28,579)	\$0.96	-
Balance December 31, 2015	1,419,327	4,171,292	\$0.33	6.57

The fair value of options granted to employees was estimated at the date of grant using the following assumptions for the years ended December 31:

	2015	2014
Expected term (years)	5.83 – 6.58 years	5.69 – 6.07 years
Volatility	34.91 – 43.52%	44.66 – 46.58%
Risk-free interest rate	1.44 – 1.85%	1.67 – 1.97%
Dividend yield	- %	- %

NOTE 13 – INCOME TAXES

The significant components of the net deferred tax asset are as follows at December 31, 2015 and 2014:

	2015	2014
Gross deferred income tax assets		
Net operating loss carryforwards	\$17,561,629	\$13,968,747
R&D credits	801,566	589,936
Property and equipment (depreciation)	(75,493)	(31,147)
Others	420,459	147,283
	18,708,161	14,674,819
Valuation allowance	(18,708,161)	(14,674,819)
Total	\$-	\$-

A valuation allowance has been recorded for the entire amount of the Company's deferred tax assets as a result of uncertainties regarding the realization of the deferred tax assets. The change in the valuation allowance totaled \$4,033,342 and \$2,602,184 for the years ended December 31, 2015 and 2014, respectively, principally due to increases in the valuation allowance associated with increased net operating losses.

As of December 31, 2015, the Company had net operating loss carryforwards for federal and state income tax reporting purposes of approximately \$45,482,439 and \$35,952,291 respectively. As of December 31, 2015 the Company also had Federal and California research and development tax credit carryforwards of approximately \$390,656 and \$410,910 respectively. The Federal net operating loss and tax credit carryforwards will expire at various dates beginning in 2025 through 2035. The California net operating loss carryforwards will expire at various dates beginning in 2016 through 2035. The California research and development tax credit carryforwards have no expiration date.

Utilization of the NOL and tax credit carryforwards may be subject to a substantial annual limitation due to ownership change limitations that may have occurred or that could occur in the future, as required by the Internal Revenue Code (the "Code"), as well as similar state provisions. In general, an "ownership change" as defined by the Code results from a transaction or series of transactions over a three-year period resulting in an ownership change of more than 50 percentage points of the outstanding stock of a company by certain stockholders or public groups.

Since the Company's formation, the Company has raised capital through the issuance of capital stock on several occasions which, combined with the purchasing stockholders' subsequent disposition of those shares, may have resulted in such an ownership change, or could result in an ownership change in the future upon subsequent disposition. The annual limitation may result in the expiration of NOL and tax credit carryforwards before utilization.

The Company has not completed a study to assess whether an ownership change has occurred or whether there have been multiple ownership changes since the Company's formation due to the complexity and cost associated with such a study, and the fact that there may be additional such ownership changes in the future. If the Company has experienced an ownership change at any time since its formation, utilization of the NOL or tax credit carryforwards to offset future taxable income and taxes, respectively, would be subject to an annual limitation under the Code, which is determined by first multiplying the value of the Company's stock at the time of the ownership change by the applicable long-term, tax-exempt rate, and then could be subject to additional adjustments, as required. Any limitation may result in expiration of all or a portion of the NOL or tax credit carryforwards before utilization.

The Company maintains a full valuation allowance for its deferred tax assets due to its historical losses and uncertainties surrounding its ability to generate future taxable income to realize these assets. Due to the existence of the valuation allowance, future changes in any unrecognized tax benefits and recognizable deferred tax benefits after the completion of an ownership change analysis is not expected to impact its effective tax rate.

The effective tax rate of the Company's provision for income tax benefit differs from federal statutory rate for the years ended December 31, 2015 and 2014, principally due to state taxes and changes in the valuation allowance.

As of December 31, 2015, and 2014, the Company had not identified any significant uncertain tax positions.

A number of the Company's tax returns remain subject to examination by taxing authorities: these include U.S. federal and state tax returns from 2005 forward.

NOTE 14 – RETIREMENT PLAN

The Company has a salary deferral plan under Section 401(k) of the Internal Revenue Code. The plan allows eligible employees to defer a portion of their compensation ranging from 1% to the maximum allowable dollar limit which is set by law. Such deferrals accumulate on a tax deferred basis until the employee withdraws the funds. The Company, at its option, may match a portion of the employees' contribution. During the years ended December 31, 2015 and 2014 the Company had not made any matching contributions.

NOTE 15 – MANAGEMENT INCENTIVE PLAN

On May 30, 2013, the Company adopted a management incentive plan that establishes a bonus pool with the objective of retaining its key employees and service providers through a potential Corporate Transaction, as defined in the plan. The plan provides for up to 7% of the total proceeds in a Corporate Transaction to be paid to key employees covered under the Plan.

NOTE 16 – SUBSEQUENT EVENTS

The Company has performed an evaluation of subsequent events through February 25, 2016 which is the date these financial statements were issued.

Corporate Governance Statement

The Board of Directors of AirXpanders Inc. (“AirXpanders” or “Company”) is responsible for the governance of the Company. Good corporate governance is a fundamental part of the culture and business practices of the Company.

The Board of Directors confirms that the Company’s corporate governance framework complies in almost all respects with the ASX’s Corporate Governance Council’s *Corporate Governance Principles and Recommendations* (3rd Edition) (“Recommendations”) and that where it does not comply, it is due to the current relative size of the Company, its stage of development, and the scale and nature of its operations. The Council recognises that different entities may legitimately adopt different governance practices, based on a range of factors, including their size, complexity, history and corporate culture.

The Company provides below a review of its corporate governance framework using the same numbering as adopted for the Recommendations.

Further details in relation to the Company’s governance framework are set out in a dedicated corporate governance information section of the Company’s website at <http://www.airxpanders.com/corporate-governance>. This section of the Company’s website contains copies of all of the corporate governance policies and Board Committee charters.

This Corporate Governance Statement was been approved by the Board of Directors of the Company on, and is current as at 11 February 2016.

Principle 1: Lay solid foundations for management and oversight

The Company did not comply with Recommendations 1.3, 1.5 or 1.6, but did comply with Recommendations 1.1, 1.2, 1.4 and 1.7, from the date of its listing on the ASX until 31 December 2015.

Recommendation 1.1:

A listed entity should disclose:

- (a) *the respective roles and responsibilities of its board and management; and*
- (b) *those matters expressly reserved to the board and those delegated to management.*

The Board's responsibilities are defined in the Board Charter, a copy of which is available at <http://www.airxpanders.com/board-charter>, and there is a clear delineation between the functions reserved for the Board and those conferred upon the Chief Executive Officer ("CEO") and certain other officers of the Company.

Recommendation 1.2:

A listed entity should:

- (a) *undertake appropriate checks before appointing a person, or putting forward to security holders a candidate for election, as a director; and*
- (b) *provide security holders with all material information in its possession relevant to a decision on whether or not to elect or re-elect a director.*

The Company will undertake checks the Board considers appropriate before appointing a person, or putting forward to security holders a candidate for election, as a director. However this will not apply to the re-election of existing directors.

Subject to any legal obligations to the contrary, the Company will provide security holders with all material information in its possession relevant to a decision on whether or not to elect or re-elect a director.

Recommendation 1.3:

A listed entity should have a written agreement with each director and senior executive setting out the terms of their appointment.

The Company has written agreements with Mr. Barry Cheskin and Mr. Dennis Condon relating to compensation for their respective roles as Chairman of the Board and Chairman of the Audit and Risk Committee.

The Company does not currently have written agreements with the other non-executive directors. The Company currently considers that there is sufficient certainty as to the terms of the non-executive directors' appointments that written agreements are not considered necessary at this stage.

The Company has written agreement with its senior executives (including the CEO) setting out the key terms and conditions of their appointment.

Recommendation 1.4:

The company secretary of a listed entity should be accountable directly to the board, through the chair, on all matters to do with the proper functioning of the board.

The Company Secretary is accountable to the Board, through the Chairman, on all matters to do with the proper functioning of the Board.

Recommendation 1.5:

A listed entity should:

- (a) *have a diversity policy which includes requirements for the board or a relevant com-*

- mittee of the board to set measurable objectives for achieving gender diversity and to assess annually both the objectives and the entity's progress in achieving them;
- (b) disclose that policy or a summary of it; and
 - (c) disclose as at the end of each reporting period the measurable objectives for achieving gender diversity set by the board or a relevant committee of the board in accordance with the entity's diversity policy and its progress towards achieving them, and either:
 - 1) the respective proportions of men and women on the board, in senior executive positions and across the whole organisation (including how the entity has defined "senior executive" for these purposes); or
 - 2) if the entity is a "relevant employer" under the Workplace Gender Equality Act, the entity's most recent "Gender Equality Indicators", as defined in and published under that Act.

The Company has adopted a Diversity Policy, however the Policy does not require the Board or a relevant committee of the Board to set measurable objectives for achieving gender diversity and to assess annually both the objectives and the Company's progress in achieving them.

As a relatively small company (amongst those listed on the ASX), the Company may face particular issues in:

- (a) establishing appropriate and measurable objectives for achieving gender diversity; and
- (b) annually reviewing and assessing those objectives and the Company's progress in achieving them, and reporting on the Company's gender diversity more generally.

The Company's operations are currently at the development and initial commercialisation stage and it has only a small number of employees. As the Company moves closer to achieving its commercialisation goals and increases its number of employees, it will re-examine its approach in this regard.

There were five men and one woman on the Board during the period between listing on ASX and the end of the 2015 financial year.

As at the date of this Corporate Governance Statement, the proportion of women in the Company as a percentage of its total employees was 24 out of 46, or 52%.

The proportion of women as a total of the senior executive positions (not including the CEO) is 4 out of 9, or 44%. For this purpose, senior executives are members of management who report directly to the CEO.

A copy of the Diversity Policy is available at <http://www.airxpanders.com/diversity-policy>.

Recommendation 1.6:

A listed entity should:

- (a) have and disclose a process for periodically evaluating the performance of the board, its committees and individual directors; and
- (b) disclose, in relation to each reporting period, whether a performance evaluation was undertaken in the reporting period in accordance with that process.

As the Company only listed on the ASX in June 2015, the Board considered it premature to undertake a formal review of the performance of the Board, its Committees and individual directors during the financial year. The Board intends to adopt a process for undertaking such reviews shortly before first undertaking them, so the Company has not yet adopted such a process.

Recommendation 1.7:

A listed entity should:

- (a) have and disclose a process for periodically evaluating the performance of its senior executives; and
- (b) disclose, in relation to each reporting period, whether a performance evaluation was undertaken in the reporting period in accordance with that process.

The Company's Board Charter requires the Board to be responsible for the evaluation of the performance of the Company's CEO. The Board Charter is available at <http://www.airxpanders.com/board-charter>.

The Board did not conduct a formal review of the CEO from the date of the Company's listing on the ASX in June 2015 until 31 December 2015 owing to the fact that the Company has a process in place whereby formal performance reviews are conducted early in the year following the end of each financial year.

The Board's process to review the performance of the CEO commences with the Board setting key objectives and performance targets for the Company and the CEO. The Nomination and Remuneration Committee will meet and assess the performance of the CEO against these objectives and agree to make a recommendation to the Board in relation to the short and long term remuneration structure of the CEO. Following feedback received from the Nomination and Remuneration Committee, the Board conducts a performance evaluation of the CEO and approves the remuneration structure of the CEO.

The CEO did not conduct a formal review of his executive team from the date of the Company's listing on the ASX in June 2015 until 31 December 2015 owing to the fact that the Company has a process in place whereby formal performance reviews are conducted early in the year following the end of each financial year.

The CEO reviews the performance of the Company's executives against key performance targets set by the CEO and based upon the CEO's key targets which have been set by the Board. Formal reviews were conducted early in 2016 in relation to the 2015 financial year.

Principle 2: Structure the Board to add value

The Company did not comply with Recommendations 2.1, 2.4 or 2.5 but did comply with Recommendations 2.2, 2.3 and 2.6, from the date of its listing on the ASX until 31 December 2015.

Recommendation 2.1:

The board of a listed entity should:

- (a) *have a nomination committee which:*
 - 1) *has at least three members, a majority of whom are independent directors; and*
 - 2) *is chaired by an independent director, and disclose:*
 - 3) *the charter of the committee;*
 - 4) *the members of the committee; and*
 - 5) *as at the end of each reporting period, the number of times the committee met throughout the period and the individual attendances of the members at those meetings; or*
- (b) *if it does not have a nomination committee, disclose that fact and the processes it employs to address board succession issues and to ensure that the board has the appropriate balance of skills, knowledge, experience, independence and diversity to enable it to discharge its duties and responsibilities effectively.*

The Board has established a Nomination and Remuneration Committee which has three members: Mr. Barry Cheskin (Chairman), Ms. Brigitte Smith and Mr. Dennis Condon. Only Mr. Condon is considered by the Board to be an independent director. Having regard to the Company's stage of development and the collective experience and expertise of the members of the Nomination and Remuneration Committee, the Board considers the current composition of the Committee to be appropriate.

The Board may reconsider the composition of its Board Committees in the future if additional independent directors are appointed.

The Nomination and Remuneration Committee Charter is available at <http://www.airxpanders.com/nomination-and-remuneration>.

The Nomination and Remuneration Committee was formed shortly before the Company listed on the ASX in June 2015 and owing to the shorter period, did not meet between the date of the Company's listing on the ASX and 31 December 2015. The Committee did however meet in early 2016 to review amongst other matters, the performance of the CEO and the Company's current remuneration policies and practices.

Recommendation 2.2:

A listed entity should have and disclose a board skills matrix setting out the mix of skills and diversity that the board currently has or is looking to achieve in its membership.

The Board has determined that, in terms of the mix of skills and diversity it is looking for in its

own membership, it is best served by having a mix of individuals with different perspectives that have deep expertise and a breadth of experience in the following areas:

- strategy and innovation;
- leading, managing and overseeing corporations in a range of industry sectors (including the health care sector), at both executive and Board level;
- financial management and corporate governance; and
- organisations with diverse governance and regulatory regimes (including private companies and international organisations).

Details in relation to the mix of skills and diversity of the Board can be found at <http://www.airxpanders.com/board-of-directors>.

Recommendation 2.3:

A listed entity should disclose:

- the names of the directors considered by the board to be independent directors;*
- if a director has an interest, position, association or relationship of the type described in [Box 2.3 of the Recommendations] but the board is of the opinion that it does not compromise the independence of the director, the nature of the interest, position, association or relationship in question and an explanation of why the board is of that opinion; and*
- the length of service of each director.*

The Board considers only Mr. Dennis Condon to be an independent director. The Board does not consider him to have any interest, position, association or relationship of the type described in Box 2.3 of the Recommendations.

The Board may in due course consider appointing further independent directors. Otherwise the Board, having regard to the Company's stage of development and the collective experience and expertise of the directors, considers its current composition to be appropriate.

The current composition of the Board and length of service of each member is as follows:

Name	Position	Date appointed	Independent	Audit & Risk Committee	Nomination & Remuneration Committee
Mr. Barry Cheskin	Chairman (non-executive)	29 December 2006	NO	NO	CHAIR
Dr. Albert Cha	Director (non-executive)	18 January 2012	NO	YES	NO
Mr. Dennis Condon	Director (non-executive)	1 August 2012	YES	CHAIR	YES
Mr. Scott Dodson	Director (executive)	22 October 2010	NO	NO	NO
Mr. Tadmor Shalon	Director (non-executive)	17 March 2005	NO	NO	NO
Ms. Brigitte Smith	Director (non-executive)	30 April 2010	NO	NO	YES

The number of meetings of the Board and Audit and Risk Committee and number of meetings attended by each of the directors from the date of listing on the ASX to the end of its 31 December 2015 financial year are as follows:

	Board Meetings		Audit & Risk Committee Meetings	
	A	B	A	B
Mr. Barry Cheskin	3	3	-	-
Dr. Albert Cha	3	3	1	1
Mr. Dennis Condon	3	3	1	1
Mr. Scott Dodson	3	3	-	-
Mr. Tadmor Shalon	3	3	-	-
Ms. Brigitte Smith	3	3	-	-

A – Number of meetings attended.

B – Number of meetings held during the time the director held office during the reporting period.

As stated above in response to Recommendation 2.1, the Nomination and Remuneration was formed shortly before the Company listing on the ASX in June 2015 and owing to the shorter period, did not meet between the date of the Company's listing on the ASX and 31 December 2015. The Committee did however meet in early 2016 to review amongst other matters, the performance of the CEO and the Company's current remuneration policies and practices.

Recommendation 2.4:

A majority of the board of a listed entity should be independent directors.

A majority of the Board was not independent during the 2015 financial year. The Board considers that only Mr. Dennis Condon is an independent director. Having regard to the Company's stage of development and the collective experience and expertise of the directors, the Board considers the current composition of the Board to be appropriate.

Recommendation 2.5:

The chair of the board of a listed entity should be an independent director and, in particular, should not be the same person as the CEO of the entity.

The roles of Chairman and CEO are performed by different persons, however the Board does not consider the Company's Chairman to be an independent director.

Having regard to the Company's stage of development and the experience of the Chairman, the Board considers the current choice of Chairman to be appropriate.

Recommendation 2.6:

A listed entity should have a program for inducting new directors and provide appropriate professional development opportunities for directors to develop and maintain the skills and knowledge needed to perform their role as directors effectively.

The Company has an induction program for new directors which provide a summary of the Company and its product and activities. The program includes one-on-one meetings with the Chairman, CEO and senior members of management. In addition, the Company is prepared to provide professional development opportunities to directors reasonably requested by directors.

Principle 3: Act ethically and responsibly

The Company complied with Recommendation 3.1 from the date of its listing on the ASX until 31 December 2015.

Recommendation 3.1:

A listed entity should:

- (a) have a code of conduct for its directors, senior executives and employees; and
- (b) disclose that code or a summary of it.

The Company has adopted a Code of Conduct which applies to all directors, executives and employees of the Company, as well as a Securities Trading Policy.

Copies of the Code of Conduct and the Securities Trading Policy are available on the Company's website at <http://www.airxpanders.com/code-of-conduct> and <http://www.airxpanders.com/corporate-governance> respectively

Principle 4: Safeguard integrity in corporate reporting

The Company did not comply with Recommendations 4.1 and 4.2 from the date of its listing on the ASX until 31 December 2015. The Company did not hold an AGM during this period; therefore Recommendation 4.3 is not applicable.

Recommendation 4.1:

The board of a listed entity should:

- (a) have an audit committee which:
 - 6. has at least three members, all of whom are non-executive directors and a majority of whom are independent directors; and
 - 7. is chaired by an independent director, who is not the chair of the board, and disclose:
 - 8. the charter of the committee;
 - 9. the relevant qualifications and experience of the members of the committee; and
 - 10. in relation to each reporting period, the number of times the committee met throughout the period and the individual attendances of the members at those meetings; or
- (b) if it does not have an audit committee, disclose that fact and the processes it employs that independently verify and safeguard the integrity of its corporate reporting, including the processes for the appointment and removal of the external auditor and the rotation of the audit engagement partner.

The Board has an Audit and Risk Committee which has two directors, both of whom are non-executive directors: Mr Dennis Condon and Dr Albert Cha. Only one member of the Committee (Mr Dennis Condon) is considered by the Board to be an independent director. Mr Condon is Chairman of the Committee and is not Chairman of the Board. The Board is of the view that at this stage of the Company's development the current composition of the Audit and Risk Committee is appropriate.

The qualifications and experience of the members of the Committee are disclosed on the Company's website at <http://www.airxpanders.com/board-of-directors>.

The Audit and Risk Committee Charter is available at <http://www.airxpanders.com/audit-and-risk-committee-charter>.

Recommendation 4.2:

The board of a listed entity should, before it approves the entity's financial statements for a financial period, receive from its CEO and CFO a declaration that, in their opinion, the financial records of the entity have been properly maintained and that the financial statements comply with the appropriate accounting standards and give a true and fair view of the financial position and performance of the entity and that the opinion has been formed on the basis of a sound system of risk management and internal control which is operating effectively.

Prior to the Board approving the Company's financial statements for the financial period ended 31 December 2015, the CEO and the Director of Finance declared in writing to the Board that, in their opinion, the financial records of the Company have been properly maintained and that the financial statements comply with the appropriate accounting standards and give a true and fair view of the financial position and performance of the Company, and that the opinion has been formed on the basis of a sound system of risk management and internal control which is operating effectively.

A CEO and CFO a declaration of this nature was not provided to the Board for the half year ended 30 June 2015, however a declaration will be provided to the Board for the half year ended 2016.

Recommendation 4.3:

A listed entity that has an AGM should ensure that its external auditor attends its AGM and is available to answer questions from security holders relevant to the audit.

The Company did not have an AGM between the date of its listing on the ASX and 31 December 2015.

Principle 5: Make timely and balanced disclosure

The Company complied with Recommendation 5.1 from the date of its listing on the ASX until 31 December 2015.

Recommendation 5.1:

A listed entity should:

- (a) have a written policy for complying with its continuous disclosure obligations under the Listing Rules; and*
- (b) disclose that policy or a summary of it.*

The Company has adopted a Continuous Disclosure Policy.

A copy of the Company's Continuous Disclosure Policy is available at <http://www.airxpanders.com/continuous-disclosure-policy>.

Principle 6: Respect the rights of security holders

The Company complied with Recommendations 6.1 to 6.4 from the date of its listing on the ASX until 31 December 2015.

Recommendation 6.1:

A listed entity should provide information about itself and its governance to investors via its website.

Information about the Company and its corporate governance is disclosed on the Company's website at <http://www.airxpanders.com>.

Recommendation 6.2:

A listed entity should design and implement an investor relations program to facilitate effective two-way communication with investors.

The Company engages an external investor relations consultant, to facilitate engagement with investors and queries which arise from time to time from security holders. The Company through its investor relations consultant, Continuous Disclosure Policy, investor newsletters, market updates, financial reporting and website, provides investors with the opportunity to have an understanding of the Company's business, governance and financial performance.

Recommendation 6.3:

A listed entity should disclose the policies and processes it has in place to facilitate and encourage participation at meetings of security holders.

The Company's Continuous Disclosure Policy sets out the Company's policies and processes to facilitate and encourage participation at meetings of security holders.

Recommendation 6.4:

A listed entity should give security holders the option to receive communications from, and send communications to, the entity and its security registry electronically.

The Company's contact details are available on its website at <http://www.airxpanders.com/contact-us>.

Security holders will be able to submit an electronic query to the Company via the website or contact its registry, Computershare, by mail, telephone, email or via online access.

All CHESS Depository Interest (CDI) holders have the option to receive communication from, and send communications to, the Company and Computershare electronically.

Principle 7: Recognise and manage risk

The Company did not comply with Recommendation 7.1, but did comply with Recommendations 7.2 to 7.4, from the date of its listing on the ASX until 31 December 2015.

Recommendation 7.1:

The board of a listed entity should:

- (a) *have a committee or committees to oversee risk, each of which:*
 - 1) *has at least three members, a majority of whom are independent directors; and*
 - 2) *is chaired by an independent director,**and disclose:*
 - 3) *the charter of the committee;*
 - 4) *the members of the committee; and*
 - 5) *as at the end of each reporting period, the number of times the committee met throughout the period and the individual attendances of the members at those meetings; or*
- (b) *if it does not have a risk committee or committees that satisfy (a) above, disclose that fact and the processes it employs for overseeing the entity's risk management framework.*

Please refer to the response to Recommendation 4.1.

Recommendation 7.2:

The board or a committee of the board should:

- (a) review the entity's risk management framework at least annually to satisfy itself that it continues to be sound; and*
- (b) disclose, in relation to each reporting period, whether such a review has taken place.*

The Board reviewed the Company's risk management framework and key risks of the Company during the financial year ended 31 December 2015 to satisfy itself that the framework continues to be sound.

Recommendation 7.3:

A listed entity should:

- (a) if it has an internal audit function, how the function is structured and what role it performs; or*
- (b) if it does not have an internal audit function, that fact and the processes it employs for evaluating and continually improving the effectiveness of its risk management and internal control processes.*

The Company does not have an internal audit function.

In conjunction with the Company's other corporate governance policies, the Company has adopted a Risk Management Policy to assist it to identify, evaluate and mitigate technological, economic, operational and other risks. The Audit and Risk Committee with oversight from the Board has responsibility to review and assess the Company's processes for evaluating and continually improving the effectiveness of its risk management and internal control processes. Management reviews and assesses the key risks of the Company together with the controls in place to mitigate these risks prior to presenting the risk management framework to the Audit and Risk Committee for review.

The Company has established a Risk Management Policy. A copy of the Risk Management Policy is available at <http://www.airxpanders.com/risk-management-policy>.

Recommendation 7.4:

A listed entity should disclose whether it has any material exposure to economic, environmental and social sustainability risks and, if it does, how it manages or intends to manage those risks.

The Board has overseen the development by management of a process to identify and manage key risks (including economic sustainability risks). These are the key risks that the directors oversee and the management team focus on when managing the business.

The Board is of the view that the Company operates in a dynamic, highly competitive industry and believes that changes in any of the following areas could have a material adverse effect on the Company's future financial position, results of operations, or cash flows; ability to obtain future financing; advances and trends in new technologies and industry standards; regulatory approval and market acceptance of the Company's products; development of sales channels; certain strategic relationships; litigation or claims against the Company based on intellectual property, patent, product, regulatory, or other factors; and the Company's ability to attract and retain employees necessary to support its growth.

The Company is not subject to material economic, environmental or social sustainability risks.

Principle 8: Remunerate fairly and responsibly

The Company did not comply with Recommendation 8.1, but did comply with Recommendations 8.2 and 8.3, from the date of its listing on the ASX until 31 December 2015.

Recommendation 8.1:

The board of a listed entity should:

- (a) *have a remuneration committee which:*
- 1) has at least three members, a majority of whom are independent directors; and
 - 2) is chaired by an independent director, and disclose:
 - 3) the charter of the committee;
 - 4) the members of the committee; and
 - 5) as at the end of each reporting period, the number of times the committee met throughout the period and the individual attendances of the members at those meetings; or
- (b) *if it does not have a remuneration committee, disclose that fact and the processes it employs for setting the level and composition of remuneration for directors and senior executives and ensuring that such remuneration is appropriate and not excessive.*

Please refer to the response to Recommendation 2.1.

Recommendation 8.2:

A listed entity should disclose policies and practices regarding the remuneration of non-executive directors and the remuneration of executive directors and other senior executives.

The Board and its Nomination and Remuneration Committee are responsible for reviewing and approving executive remuneration and incentive policies and practices. The Company has a clear distinction between the structure of non-executive directors' remuneration and that of executive directors and senior executives.

Disclosure in relation to the Company's stock incentive plan that provides for the issuance of incentive and non-qualified stock options to employees and directors is provided in the Annual Report.

All senior executives of the Company are subject to an annual performance review. Each year the CEO sets senior executive key performance targets. These targets are aligned to the overall business goals and the Company's requirements. In the case of the CEO, these key performance targets are negotiated between the CEO and the Board. The Nomination and Remuneration Committee reviews the evaluation process as required. Short term and long term incentives are dependent on the outcome of these evaluations. All equity based rewards require the approval of the Board.

The fees paid by the Company to its non-executive directors are as follows:

- US\$8,000 per month to the Chairman of the Board; and
- a further US\$5,000 per annum to the Chairman of each of the Audit and Risk Committee and the Nomination and Remuneration Committee.

No other fees are currently paid to the non-executive directors. Directors may however be reimbursed for travel and other expenses incurred in attending to the Company's affairs.

Recommendation 8.3:

A listed entity which has an equity-based remuneration scheme should:

- (a) *have a policy on whether participants are permitted to enter into transactions (whether through the use of derivatives or otherwise) which limit the economic risk of participating in the scheme; and*
- (b) *disclose that policy or a summary of it.*

The Company's Securities Trading Policy prohibits participants in the Company's share or option plans or who otherwise hold securities in the Company from engaging in any conduct that seeks to secure the economic value attaching to the relevant securities and remove the element of price risk inherent in the value of those securities, while the securities remain unvested or subject to escrow. Please refer to the Policy for further details.

A copy of the Policy is available at <http://www.airxpanders.com/corporate-governance>.

Shareholder information

Overview

The Company has securities listed for quotation in the form of CHESS Depository Interests (CDIs) on the Australian Securities Exchange (ASX) that trade under the symbol "AXP".

Each share of Class A common stock (Share) is equivalent to 3 CDIs.

The information below was applicable as at 26 February 2016.

The Company's share capital is as follows:

Type of Security	Number of Securities
Total number of issued Shares (1)	70,427,195
Total number of issued CDIs	75,812,145
Total number of CDIs assuming all Shares held as CDIs	211,281,585

(1) Includes Shares held by CHESS Depository Nominees Pty Limited (CDN).

Substantial holders

The names of substantial holders in the Company and their respective equity holdings (to the best of the Company's knowledge) follow below:

Name	Date of becoming a substantial holder	Number of equity securities	Percentage of voting power
Vivo (1)	18 January 2012	16,842,159 Shares (equivalent to 50,526,477 CDIs)	23.9%
GBS Venture Partners Pty Ltd as Trustee for the GBS Bioventures IV Trust	21 April 2010	5,489,067 CDIs 14,272,556 Shares (equivalent to 42,817,668 CDIs)	22.9%
Prolog Capital II, L.P.	13 March 2009	6,778,169 Shares (equivalent to 20,334,507 CDIs)	9.6%
J P Morgan Nominees Australia Limited (2)	29 June 2015	12,454,106 CDIs	5.9%

(1) Vivo includes: Vivo Ventures VII, L.P. (16,482,917 Shares – equivalent to 49,448,751 CDIs) and Vivo Ventures VII Affiliates Fund, L.P. (359,242 Shares - equivalent to 1,077,726 CDIs)

(2) The Company is not aware of the extent (if any) to which the holding of J P Morgan Nominees Australia Limited is subject to an exception listed in section 609 of the Corporations Act.

For the purpose of the above table, a “substantial holder” is a security holder, who together with their associates, have a relevant interest (within the meaning of section 608 of the Corporations Act) in securities representing 5% or more of the total number of votes attached to voting shares in the Company.

(3) Consists of (i) 16,482,917 Shares held by Vivo Ventures Fund VII, LP and (ii) 359,242 Shares held by Vivo Ventures VII Affiliates Fund, LP. Vivo Ventures VII, LLC is the sole general partner of each Vivo Ventures Fund VII, LP and Vivo Ventures Affiliates Fund LP. Dr Cha is one of three managing members of Vivo Ventures VII LLC and may be deemed to have shared voting and dispositive power over the Shares. Dr Cha disclaims beneficial ownership of such Shares except to the extent of any pecuniary interest therein.

(4) Consists of (i) 60,000 Shares held directly by Mr Shalon and (ii) 441,446 Shares held amongst six trusts established for the benefit of members of Mr Shalon's family.

Distribution Schedules

The following table is a distribution schedule of the number of holders of CDIs and Shares (as-converted to CDIs) as at 26 February 2016:

Category	Number of Holders
1-1,000	76
1,001 – 5,000	171
5,001 – 10,000	124
10,001 – 100,000	247
100,001 and over	64
Total	682⁽¹⁾

(1) Includes 636 holders of CDIs and 46 holders of Shares (excluding CDN). Note: No holders hold both CDIs and Shares.

Unmarketable Parcels

There were 21 holders of CDIs and Shares (as-converted to CDIs) holding less than a marketable parcel of CDIs (being a parcel of securities not less than \$500).

Top 20 Holders

Set out below is a schedule of the 20 largest holders of securities (CDIs and Shares, as-converted to CDIs) in the Company, including the number and percentage held by those holders as at 26 February 2016. [Related but separate legal entities are not aggregated for the purposes of the table below.]

	Name of registered holder	Number (or equivalent number) of CDIs held	Percentage
1	VIVO VENTURES FUND VII LP	49,448,751	23.4%
2	GBS VENTURE PARTNERS TR GBS BIOVENTURES IV TRUST DTD APRIL 24 2008	48,306,735	22.9%
3	PROLOG CAPITAL II LP	20,334,507	9.6%
4	J P MORGAN NOMINEES AUSTRALIA LIMITED	12,454,106	5.9%
5	UBS NOMINEES PTY LTD	9,219,412	4.4%
6	HERON CAPITAL VENTURES FUND ILP	7,962,513	3.8%
7	CORRELATION VENTURES LP	7,565,481	3.6%

Top 20 Holders (continued)

8	HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED	7,192,189	3.4%
9	NATIONAL NOMINEES LIMITED	6,730,917	3.2%
10	CITICORP NOMINEES PTY LIMITED	5,105,876	2.4%
11	BRISPOT NOMINEES PTY LTD <HOUSE HEAD NOMINEE NO 1 A/C>	3,377,649	1.6%
12	CS FOURTH NOMINEES PTY LIMITED <HSBC CUST NOM AU LTD 11 A/C>	2,644,210	1.3%
13	BOND STREET CUSTODIANS LIMITED <LAM1 - D08047 A/C>	1,700,000	0.8%
14	BNP PARIBAS NOMINEES PTY LTD <AGENCY LENDING DRP A/C>	1,494,634	0.7%
15	RBC INVESTOR SERVICES AUSTRALIA NOMINEES PTY LIMITED <PISELECT>	1,182,916	0.6%
16	VIVO VENTURES VII AFFILIATES FUND LP	1,077,726	0.5%
17	SANDHURST TRUSTEES LTD <AUSTRALIAN NEW HORIZONS A/C>	1,003,533	0.5%
18	PODESTA FAMILY GROUP PTY LTD <PODESTA FAMILY GROUP A/C>	1,000,000	0.5%
19	GOLD TIGER INVESTMENTS PTY LTD	600,000	0.3%
20	MR ALEXANDER JAMES WENTWORTH HILL	600,000	0.3%
	Name of registered holder	Number (or equivalent number) of CDIs held	Percentage
	Totals: Top 20 holders of Securities	189,001,155	89.5%
	Total Remaining Holders Balance	22,280,430	10.5%
	Total Number (or equivalent number) of CDIs held	211,281,585	

Options (not listed on ASX)

As at 26 February 2016, there were 4,171,792 options on issue to purchase Shares (Options) (equivalent to 12,515,376 CDIs) under the Company's 2005 Equity Incentive Plan and 2015 Equity Incentive Plan. The number of holders of Options at 26 February 2016 was 57.

The following table is a distribution schedule of the number of holders of Options (as-converted to CDIs) as at 26 February 2016:

Category	Number of Holders
1-1,000	
1,001 – 5,000	
5,001 – 10,000	
10,001 – 100,000	
100,001 and over	
Total	57

Warrants (not listed on ASX)

As at 26 February 2016, there were 469,970 warrants to acquire a total of 469,970 Shares (Warrants) (equivalent to 1,409,910 CDIs). The number of holders of Warrants at 26 February 2016 was 13. [Oxford Finance Funding I, LLC holds 160,000 Warrants and is the only holder with more than 20% of the total number of warrants.]

The following table is a distribution schedule of the number of holders of Warrants (as-converted to CDIs) as at 26 February 2016:

Category	Number of Holders
1-1,000	
1,001 – 5,000	
5,001 – 10,000	
10,001 – 100,000	
100,001 and over	
Total	13

ASX restrictions

The number of Shares, Options and CDIs subject to ASX restriction and the restriction period applying to those Shares, Options and CDIs is as follows:

Restriction period	Number of restricted securities
Until 11 June 2016	40,425 Shares
	58,290 CDIs
Until 22 June 2017	827,758 Shares
	2,856,452 Options

Voluntary escrow

The number of Shares, Options, Warrants and CDIs subject to voluntary restriction and the restriction period applying to those Shares, Options, Warrants and CDIs is as follows:

Escrow period	Number of escrowed securities
Until 22 June 2016	32,324,172 Shares
	2,079,117 CDIs
	343,324 Options
	111,117 Warrants
Until 22 June 2017	10,774,730 Shares
	693,039 CDIs
	114,441 Options
	37,039 Warrants

Voting Rights

Every holder of Shares present in person or by proxy is entitled to one vote for each Share held on the record date for the meeting on all matters submitted to a vote of Shareholders.

CDI Holders may attend and vote at AirXpanders' general meetings. The Company must allow CDI Holders to attend any meeting of Shareholders unless relevant US law at the time of the meeting prevents CDI Holders from attending those meetings.

In order to vote at such meetings, CDI Holders may:

- instruct CDN, as the legal owner, to vote the Shares underlying their CDIs in a particular manner. A voting instruction form will be sent to CDI Holders with the notice of meeting or proxy statement for the meeting and this must be completed and returned to the Registry before the meeting;
- inform AirXpanders that they wish to nominate themselves or another person to be appointed as CDN's proxy for the purposes of attending and voting at the general meeting; or

- convert their CDIs into a holding of Shares and vote these at the meeting. Afterwards, if the former CDI Holder wishes to sell their investment on the ASX it would need to convert the Shares back to CDIs. In order to vote in person, the conversion from CDIs to Shares must be completed before the record date for the meeting.

One of the above steps must be undertaken before CDI Holders can vote at Shareholder meetings.

Proxy forms, CDI voting instruction forms and details of these alternatives will be included in each notice of meeting or proxy statement sent to CDI Holders by AirXpanders.

Holders of issued but unexercised options and warrants are not entitled to vote.

Required Statements

- There is no current on-market buy-back of the Company's securities.
 - The Company is incorporated in the state of Delaware in the United States of America.
 - The Company is not subject to Chapters 6, 6A, 6B and 6C of the Corporations Act 2001 (Cth) dealing with the acquisition of shares (ie, substantial holdings and takeovers).
 - The Company's securities are not quoted on any exchange other than the ASX.
 - Under the Delaware law, shares are generally freely transferable, subject to restrictions imposed by US federal or state securities laws, by a company's certificate of incorporation or by-laws, or by an agreement signed with the holders of the shares at issue. The Company's amended and restated certificate of incorporation and amended and restated by-laws do not impose any specific restrictions on transfer.
 - The Company has used the cash (and assets in a form readily convertible to cash) that it had at the time of admission to the ASX in a manner consistent with its business objectives (as described in the Prospectus lodged with the Australian Securities and Investments Commission with respect to the Company's initial public offering) from the time of admission to the ASX in June 2015 through to 31 December 2015.
 - The name of the Australian Secretary is Brendan Case, and the name of the US Secretary is John Lai.
 - The address and telephone number of our principal registered office in Australia is:
Level 13, 41 Exhibition Street
Melbourne, Victoria 3000
+ 61 410 442 393
 - The address and telephone number of our office in the United States, which is our principal administrative office, is:
1047 Elwell Court
Palo Alto, California 94303
+1 650 390 9000
 - Register of CDIs:
Computershare Investor Services Pty Ltd
GPO Box 2975, Melbourne Victoria 3001, Australia
Telephone: 1300 850 505 (within Australia) or +61 3 9415 4000 (outside Australia)
- Register of Shares:
Computershare, Inc.
250 Royall Street, Canton, MA 02021, United States of America
Telephone: +1 800 962 4284

Corporate Directory

Board of Directors

Mr Barry Cheskin, Chairman
Mr Scott Dodson, President and CEO
Ms Brigitte Smith, Non-executive Director
Dr Albert Cha, Non-executive Director
Mr Teddy Shalon, Non-executive Director
Mr Dennis Condon, Non-executive Director

Executive Team

Mr. Scott Dodson, President & CEO
Mr. Anthony Carnemolla, VP of Sales
Mr. Tony Morefield, VP of Operations & Manufacturing
Ms. Naghmeh Nouri, VP of Quality and Regulatory Affairs
Ms. Gwen Drain, Senior Director of Human Resources
Ms. Kathy Kelly, Senior Director of Clinical Affairs
Ms. Jennie Kim, Senior Director of Global Marketing
Mr. John Lai, Senior Director of Finance
Mr. Mark Payne, Senior Director of Research & Development
Mr. Gary Jones, Director of Customer Relations

Company – US Office & Headquarters

AirXpanders Inc.
1047 Elwell Court
Palo Alto, California 94303
United States of America
Telephone: +1 650 390 9000
www.airxpanders.com

Company - Registered Office in Australia

c/- Case Corporate Governance Pty Ltd
Level 13, 41 Exhibition Street
Melbourne, Victoria 3000
Australia

Auditor

SingerLewak LLP.
100 West San Fernando Street, Suite 275
San Jose, California 95113
United States of America
Telephone: +1 408 294 3924
www.singerlewak.com

CDI Registry

Computershare Investor Services Pty Ltd
GPO Box 2975, Melbourne Victoria 3001,
Australia
Telephone: 1300 850 505 (within Australia)
or +61 3 9415 4000 (outside Australia)

Investor Relations

Kyahn Williamson
Buchan Consulting
Tel: +61 (3) 9866 4722 / + 61 (0)401018828
Email: kwilliamson@buchanwe.com.au

Annual General Meeting Date & Place

The Annual Meeting of Stockholders of the Company will be held at Johnson Winter & Slattery's Sydney office at Level 25, 20 Bond Street Sydney, New South Wales, Australia on Tuesday, 17 May 2016 at 9.00am Australian Eastern Standard Time (Monday, 16 May 2016 at 4.00pm U.S. Pacific Standard Time).

Australian legal advisor

Johnson Winter & Slattery
Level 25, Bond Street
Sydney, New South Wales 2000
Australia
Telephone: +61 2 8274 9555
www.jws.com.au

US legal advisor

Cooley LLP.
3175 Hanover Street, Palo Alto, California
94304-1130
United States of America
Telephone: + 1 650 843 5000
www.cooley.com

ASX Code

AXP



ABN: 28 604 398 423

Address: Level 13, 41 Exhibition St,
Melbourne VIC 3000

Customer Service: 1-800-778-662
Email: info@airxpanders.com

