



Graham Carrick  
The first commercial cochlear  
implant recipient (1982)



Hear now. And always

Cochlear®

This year marks the 30th anniversary of the first commercial multichannel cochlear implant. The recipient, Graham Carrick, was 37 in 1982 and profoundly deaf. Graham finds it hard to explain quite how much the implant has changed his life, but he is clear that nearly every aspect of it, from his family life, to his social life to his career, has improved more than he ever thought possible.

Since that first implant, Cochlear has delivered the gift of sound to more than a quarter of a million people around the world. Our hearing solutions have helped people of all ages from all walks of life reconnect to families, friends and communities.

To our recipients, we are a lifelong hearing partner and remain committed to delivering advanced solutions and ongoing support, to ensure a lifetime of the best possible hearing.

Hear now. And always



1982

Graham hearing his daughter's voice shortly after implantation

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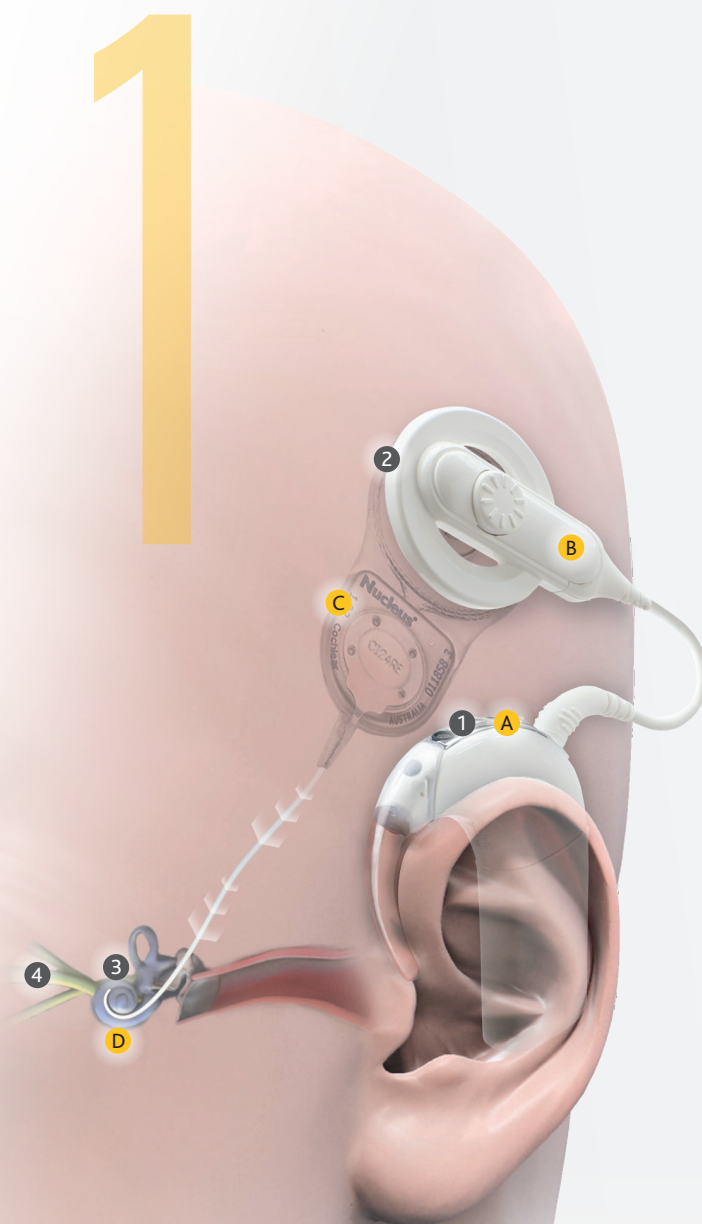
*I'm happier  
than I ever was.  
It brought me back  
to who I used to be.*

2012

Graham with daughter  
Heather 30 years on



We offer three advanced solutions to address different types of hearing loss, and upgrades without the need for further surgery.



## OUR THREE PRODUCTS

## COCHLEAR™ NUCLEUS® SYSTEM

### Type of hearing solution

### Electrical stimulation

### How our implantable hearing solutions work

The ear is implanted with a cochlear implant system which has both external and internal parts:

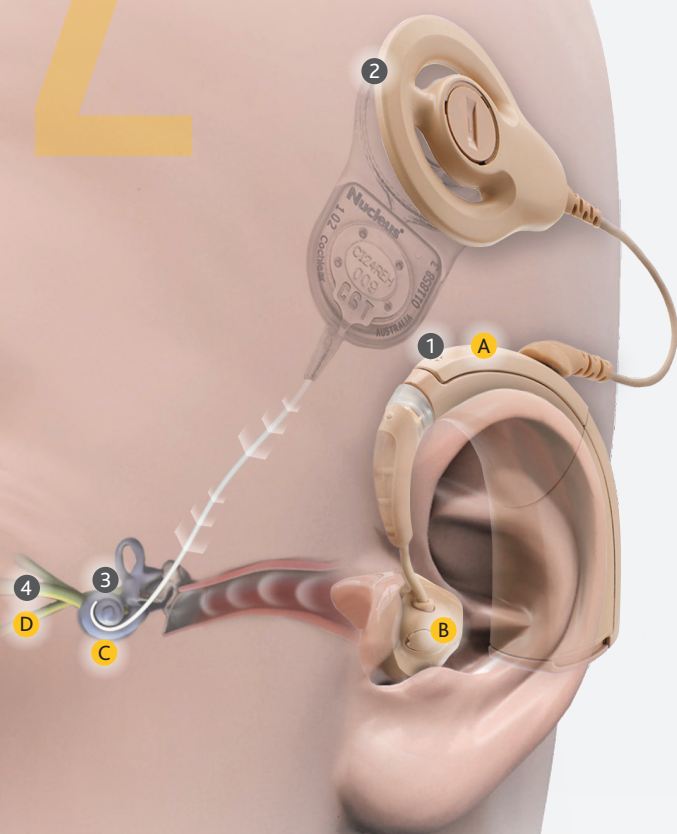
- A. the sound processor and
- B. the coil are worn behind the ear; and
- C. the implant is placed just under the skin, behind the ear; and
- D. the electrode array is positioned in the cochlea.

Cochlear implants in both ears result in a more balanced sound which makes it easier to understand speech in noisy environments or locate where sound is coming from.

How the cochlear implant system works

1. The sound processor captures sound and converts it into digital code.
2. The sound processor transmits the digitally coded sound via the coil to the implant just under the skin.
3. The implant converts the digitally coded sound to electrical signals and sends them to the electrode array.
4. The implant's electrodes stimulate the hearing nerve which relays the sound to the brain.

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### COCHLEAR™ HYBRID™ SYSTEM

#### Electro-acoustic stimulation

##### Acoustic pathway

- A. The external sound processor sends low frequency sounds to the acoustic component.
- B. The acoustic component amplifies the low frequency sounds and sends them via the normal hearing pathway.
- C. The amplified sounds activate the hearing nerves.
- D. The nerve hearing response caused by acoustic stimulation is sent to the brain which combines with electrical stimulation into a perceived sound.

##### Electrical pathway

1. The sound processor captures sound and converts it into digital code.
2. The sound processor transmits the digitally coded sound via the coil to the implant just under the skin.
3. The implant converts the digitally coded sound to electrical signals and sends them to the electrode array, which is positioned in the cochlea.
4. The implant's electrodes stimulate the hearing nerve which relays the sound to the brain.

3



### COCHLEAR™ BAHÁ® 3 SYSTEM

#### Bone conduction

##### The Baha System combines:

- A. a small titanium implant;
- B. a connecting abutment; and
- C. a detachable high performance sound processor.

The implant osseointegrates with bone (implant and bone merge), allowing sound to be conducted directly to the cochlea. Sounds can be heard clearly because the damaged portions of the ear – outer or middle – are bypassed.

##### How the bone conduction implant system works

1. A sound processor picks up sound vibrations.
2. A connecting abutment transfers sound into mechanical vibrations from the Baha device to the implant.
3. A small implant, which is placed in the bone behind the ear, fuses with the living bone. This implant transfers the sound vibrations, via the skull, directly to the functioning cochlea.

# Advanced hearing solutions

## Cochlear Baha

The Cochlear Baha 3 System continues to set performance benchmarks in direct bone conduction hearing.

In F12, the Baha BP110 Power Sound Processor continued its global rollout. The reliability and performance of the BP110 Power have been well received in the market, with studies showing that it provides better hearing performance over previous generation processors<sup>1,2</sup>.

At the end of F12, the Company received CE Marking approval for the next generation Cochlear Baha BA400 Abutment, which is designed to improve soft tissue stability, leading to better patient outcomes and a reduction in surgery time. The BA400 will be released commercially to selected clinics in Europe in early F13. United States Food and Drug Administration (FDA) approval is expected in F13, followed by full commercial availability later in that financial year.



## Nucleus CI422 with Straight Electrode

In F12, the Cochlear Nucleus CI422 with Slim Straight electrode, the world's thinnest full length electrode, was launched in Australia, the Americas and Asia Pacific.

Clinical studies verify excellent patient hearing preservation and hearing performance with the Slim Straight and confirm a substantial improvement in speech and hearing in noise<sup>1,2,3</sup>. The electrode also suits a range of surgical approaches, making it a popular choice for surgeons.

The addition of the new Slim Straight further strengthens Cochlear's unique electrode portfolio and is testament to the Company's ongoing collaboration with surgeons and hearing health professionals to help meet the individual needs of recipients.



- 1 Pffner F, Caversaccio MD and Kompis M. Comparisons of sound processors based on osseointegrated implants in patients with conductive or mixed hearing loss, 2011.
- 2 Flynn MC, Hedin A, Halvarson G, Good T and Sadeghi A. Hearing performance benefits of a programmable power Baha sound processor with a directional microphone for patients with a mixed hearing loss, 2012.

- 1 Skarzynski H, Lorens A, Matusiak M, Porowski M, Skarzynski PH and James CJ. Partial Deafness Treatment with the Nucleus Straight Research Array Cochlear Implant. Audiology and Neurotology, 2012.
- 2 Lesinski-Schiedat A, Buechner A, Schuessler M and Lenarz T. Hybrid-L and CI422 for treatment of partial deafness. Medizinische Hochschule Hannover (MHH), 2011.
- 3 Briggs RJS, Plant KL, English R, Hollow R and Cowan R. Initial Clinical Experience with the Nucleus Straight Research Array CI422. The 8th Asia Pacific Symposium on Cochlear Implant and Related Sciences, 2011.

### Cochlear Nucleus

Cochlear's hearing solutions are designed to give recipients the best possible hearing outcomes for the lives they lead.

The Nucleus CP810 Sound Processor contains our unique Dual-Microphone technology and advanced sound input processing technologies that are designed to improve recipients' hearing in a wide range of environments. It is also water-resistant and highly durable and has easy to use buttons for maximum convenience.

The Nucleus CR110 Remote Assistant is the industry's only bi-directional hand held remote assistant, which helps recipients manage their hearing more easily and helps parents of young recipients check their children's systems are working properly, for extra peace of mind.



# Cochlear has increased the final dividend to \$1.25 a share, making an increase for the year of 9%

The past financial year has been a period in two parts. A successful and momentum building first three months and then a very challenging and sobering time following the voluntary recall of CI500 series implants in September 2011.

The recall impacted the whole Cochlear family, most of all our healthcare providers and many of our recipients, as well as our staff. We are very conscious of their difficulties and appreciate their understanding as we did our very best to respond to the recall and its consequences. Together, we worked through a complex range of issues and we continue our commitment to improve the lives of the hearing impaired.

## Results

Cochlear achieved a credible 2012 financial year (F12) result in the context of the recall. Revenue in constant currency was up 1%, but net profit after tax fell to \$56.8 million, reflecting the significant charge to profit of \$138.8 million for recall costs before tax.

## Dividends

At the AGM in October 2011, I reported that it was the Board's intention to support shareholders through the recall process by at least maintaining the dividend at existing levels. This we did and in March 2012, we paid an interim dividend of \$1.20 per share, unchanged on the September 2011 payment.

In view of the strong ongoing cash flows generated by Cochlear in F12 and given a positive outlook over the longer term, the Board has determined to increase the final dividend to \$1.25 a share, making an increase for the year of 9%. The Company has now increased its dividend each year since listing in 1995.

We will continue to monitor both free cash flow and earnings as we make future dividend decisions and will strive to manage carefully the impact of the recall on the Company's financial stability and the ability to look after our shareholders through the dividend process.

As tax paid in Australia was lower this year, the franking is reduced to 35% (F11 final dividend franked to 70%).

## World economic conditions

Cochlear is a global company with a direct presence in over 20 countries and sales into over 100 countries. World events have an impact on our results, as do fluctuating foreign exchange rates.

Cochlear's portfolio of products and geography are important in managing our overall performance in an uncertain world. Inevitably, some countries are better placed for growth than others, but together the mix is well placed to deliver sustainable growth.

The continued economic uncertainty in Europe during F12 impacted the growth in certain developed countries, but reimbursement levels in the major countries have been maintained.

The emerging markets continue to be a focus and accounted for 34% of unit sales in F12 (up from 24% in the 2002 financial year). These markets, particularly China and India, continue to be a focus.

Negative foreign exchange impacts continued to be significant in F12. Cochlear has a comprehensive hedging strategy that assists in smoothing currency fluctuations in the short term, but the continued strength of the Australian dollar against the major operating currencies has been and will be a continual headwind.

Cochlear's net profit after tax would have been \$23.7 million higher in F12 if F11 foreign exchange rates had prevailed.

## Director and Board activities

The Board has played a major role in the oversight of the recall activities. In particular, the Medical Science Committee has taken on additional responsibilities in monitoring the progress of the recall. Under the experienced leadership of director Prof Byrne, the Medical Science Committee formally met 15 times during the year and its members also frequently met with executives outside of the Committee meetings to understand the detail of this complex and multifaceted issue.

In addition, we have had regular updates on the impact of the recall on other parts of the business. The Board has been insistent that the recall is dealt with in an urgent and transparent manner, but at the same time, it is critical that the ongoing business operations continue to operate at a high level.

I believe the Board has worked hard and diligently in difficult circumstances and I thank them for their teamwork and effort. Notwithstanding that effort, we will not consider changing the current directors' fee structure until we see a more stable financial performance, and then we will review fees in terms of fair market levels based on that future situation.

To further understand the impact of the recall events and how the business and market were responding, I undertook a comprehensive tour of our worldwide operations. I believe the right balance has been reached between ongoing operations and comprehensively dealing with the recall.

I believe we have made every attempt to deal openly with the recall issues and have accepted our responsibilities face on. I thank all our team members for their commitment to a difficult task, and our recipients for their understanding.

I am also pleased to see that we continue extending our commitment and orientation to recipient services and believe that is an important part of achieving our longer term objectives and success.

During my trip, I was made aware of new early stage but credible research concerning hearing and dementia. This research suggests the importance of a hearing strategy as a major component of adult health management. If there is, in fact, a relationship between maintaining hearing and delaying dementia, then this could have longer term implications for our adult market. Chris Roberts covers this more fully in his CEO/President's Report.

### Our people

Cochlear employs approximately 2,500 people in some 25 countries. In our Australian operations alone, we are represented by over 60 nationalities.

This diversity has been a feature of Cochlear's workforce since the Company's inception. The global understanding that it brings has been an important element in Cochlear's success.

I would like to thank all our employees for their dedication, passion and hard work over the last year. The extra work created by the recall has been handled well and I am proud of the contribution everyone has made to ensuring that recipients remain our priority.

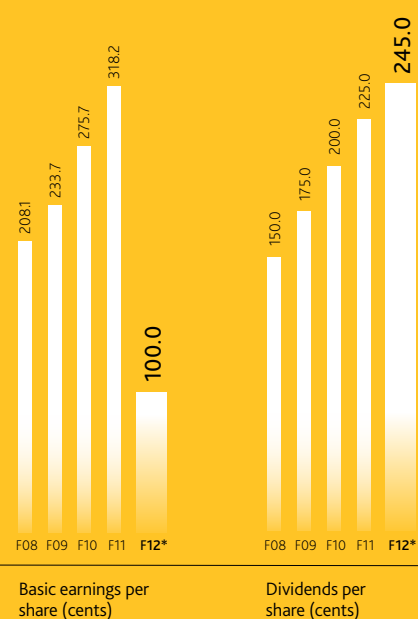
### Conclusion

F12 was a difficult year for the Company, but we have maintained an ongoing focus on retaining our long-term market leadership.

I still believe Cochlear is well positioned for the longer term but we need to be diligent and attentive as we continue on a challenging journey.



Mr Rick Holliday-Smith Chairman



\* Financial years.

# F12 was a challenging year, but one which leaves us stronger as we enter F13

F12 was characterised by decisive action taken in September 2011 to recall unimplanted Nucleus CI500 series implants and switch the implant component in Cochlear's flagship cochlear implant system to the Nucleus CI24RE implant. Given an increase in observed field failures of CI500 series implants, a quick decision was in the best interest of recipients, and hence all stakeholders.

The ramp-up of CI24RE manufacturing (and consequences along the entire supply chain), management of inventory such that no surgeries were missed, and extensive communication and support, particularly by Cochlear's field staff, were critical success factors. Cochlear's people and partners worked closely with healthcare professionals globally managing a difficult situation. To all those people who helped and supported the situation, thank you. To all the healthcare professionals who were inconvenienced, we apologise and thank you for your support and understanding. And to those implant recipients who experienced an implant failure, we apologise unreservedly. We are committed to supporting our recipients for life, and our promise "Hear now. And Always" is very important to us.

Swapping the CI500 series implants for the CI24RE implant in the Nucleus cochlear implant system does not compromise hearing performance because the two implants provide identical hearing performance when used with the Nucleus CP810 Sound Processor (Nucleus 5 externals). The Nucleus 5 externals, released in 2009, have been very well received by recipients globally. For example, Dual-Microphone technology, along with advanced pre-processing of sound, provides unmatched hearing performance particularly in difficult hearing conditions such as speech in noise. In addition, ergonomics, cosmesis, and usability of the system have been embraced by our recipients. Overall, the swap of CI500 series implants to CI24RE implant was well accepted in the market with minimal market share loss.

For a number of months post recall, inventory of the CI24RE was limited, and while no surgeries were missed, there was destocking of inventory from hospital shelves. Cochlear implant unit sales for F12 were 23,087 units, down 6% on F11. We also experienced a reduction of tender sales in the People's Republic of China (PRC) where no cochlear implants were supplied to donation or national tender markets - this was unrelated to the CI500 series recall, as the CI500 has never been sold in the PRC.

## Financial results

Total revenue for F12 was \$779.0 million, down 4% over F11. An appreciating Australian dollar (average rates in F12 up 5% against the USD and 5% against the Euro) masked underlying sales growth, with sales in constant currency (e.g. restating F11 at F12 FX rates) up 1%.

Net profit after tax was \$56.8 million, down 68%. This was after an expense provision of \$138.8 million for the CI500 series recall (\$101.3 million after tax).

Bone Anchored Solutions (BAS) product sales (e.g. Baha) were \$77.9 million (down 4% in constant currency). This result was impacted by distraction from the cochlear implant recall as well as increased competition in the bone conduction segment. The BAS team continues innovating, and global launch of the Baha 3 Power was successfully completed in F12, with more innovation planned for F13.

In constant currency terms, the Americas sales of \$297 million were down 2%, with EMEA (Europe, Middle East and Africa) up 2% to \$285 million, and Asia Pacific with sales of \$123 million up 4%.

Free cash flow of \$143 million, down on the \$166 million free cash flow in F11, was impacted by the recall. F12 debtor days at 73 days were similar to the 74 days at the end of F11, while F12 inventory levels at \$101.3 million (182 days) was down 5% from F11 (\$106.1 million (173 days)). The balance sheet remains strong, with net cash at 30 June 2012 of \$3 million (and \$128 million of a \$200 million facility unused). The final dividend was increased 4% to \$1.25 per share, giving a full year dividend of \$2.45 per share, up 9%.

## Growth through helping people hear

Cochlear enters F13, a stronger, improved company with an exciting pipeline of products and opportunities to drive growth over many years.

There remains a large unmet clinical need in terms of people with a significant hearing loss requiring implantable technology such as cochlear implants or bone conduction implants. Hearing is not only important for language and communication; for adults, maintaining hearing is integral to healthy ageing. Hearing loss is an independent risk factor for cognitive decline. Data published by Lin et al<sup>1</sup> in 2011 looked at 10 year follow-up data on 639 adults in the Baltimore Longitudinal Study of Ageing. These data showed that even after correcting for various risk factors (such as age, gender, smoking and the like), a mild hearing loss doubled the risk of developing dementia, a moderate loss trebled the risk and a severe loss increased the risk of developing dementia by a factor of five. The brain remains neuroplastic over one's life, and the adage "use it or lose it" is a reminder to all about the consequences of hearing loss. Encouragingly, in the developed economies, cochlear implantation in the over 65s is the fastest growing demographic. Indeed, in countries such as the USA, Germany and Australia, there were more new recipients over the age of 65 than children receiving cochlear implants in those countries. Cochlear implantation is for all ages.

Another important clinical trend includes the benefits of preserving auditory structure and function and combining acoustic amplification (at lower frequencies) with electrical stimulation (at higher frequencies). Bilateral cochlear implantation remains an important trend, driven by excellent clinical outcomes, as does the growth in children receiving cochlear implantation in the developing economies.

With Cochlear's market leadership, strong balance sheet and global footprint, there remains significant opportunity for Cochlear to address these global trends. Technologic innovation remains key, and research and development was up 10% to \$119 million for F12. Technological building blocks, including new chipsets, new electrodes, wireless communication, transducers for acoustic implants, implantable microphones, implantable power sources and the like, form the basis for a range of products being developed.

Cochlear implantation as an intervention is very multidisciplinary, much more so than many other medical device areas, and placing Cochlear within a hearing precinct at Macquarie University helps ensure Cochlear remains close to advances relevant to the field.

#### Aligning stakeholders interests: total shareholder return

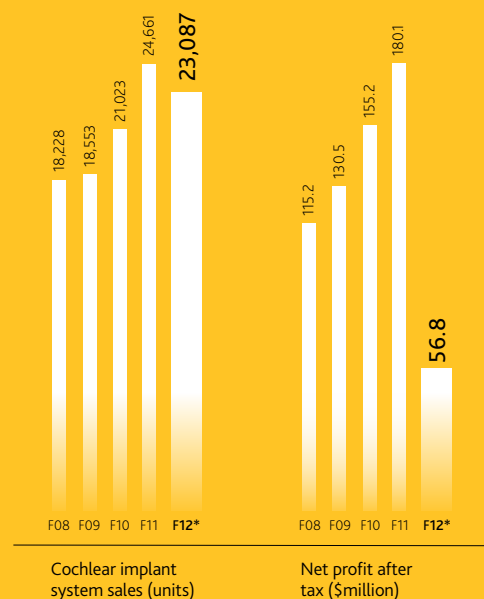
The business of developing, manufacturing and supplying implantable devices for the hearing impaired, involves a lifelong commitment of support to recipients. For example, ensuring future external sound processors are backwards compatible to previous generation implants is fundamental to making sure each recipient has a lifelong benefit from the implant. This lifelong commitment we take very seriously, hence our tag line: "Hear now. And always." This means, for example, that the long-term consequences of seemingly short-term decisions must be factored into everything we do.

From a shareholder perspective that is good news, as the day-to-day business is truly about balancing the short and long term. It also makes it easier to ensure our business plans are linked with what drives shareholder returns. Total shareholder return (TSR) (both absolute and relative) is a key management metric. Three year TSR is one of the performance hurdles for management's long-term incentive program (specifically TSR relative to the S&P/ASX 100). Three year TSR to 30 June 2012 was 24.1%, which placed Cochlear 36th out of the S&P/ASX 100 companies. While there are many variables impacting share price over which management has no control, over the longer term share price does reflect management actions, and significant thought is given to connecting business strategy with shareholder returns.

Finally, and as expressed in the past, the passion and commitment of the 2,500 employees of Cochlear are palpable, and remain a key success factor for Cochlear, and to all our employees, thank you. There is no less passion and commitment in the thousands of healthcare professionals globally that implant and support our products. Together, we truly change the world of the hearing impaired.



Dr Chris Roberts CEO/President



# Sales revenue was up 1% in constant currency. Recall costs of \$138.8 million were recognised

## Sales up in constant currency

- Total revenue down 4% to \$779.0 million.
- In constant currency terms, sales revenue up 1%.
- Sales of cochlear implant units were down 6% to 23,087. Unit sales in the second half of the current financial year were up 15% over the first half.
- Revenues in constant currency terms increased in EMEA 2% and Asia Pacific 4% but were down in Americas 2%.
- The portfolio effect of selling in over 100 countries was still evident this year. There were no donation or tender sales in China in the current year (2011: approximately 1,000 units).
- Destocking of approximately 1,000 units followed the CI500 series implant recall.

## Recall costs

- The CI500 series of implants was recalled in September 2011.
- Recall costs of \$138.8 million were recognised in the current year as a charge to cost of sales (\$101.3 million after tax).

## Profit

- Gross margin (excluding product recall expense of \$138.8 million) to total revenue at 74% was two percentage points above last year. This was driven by the mix of sales to higher priced markets and manufacturing efficiency and cost containment.
- Selling, general and administration expenses were up just 1% (4% in constant currency) as a result of a disciplined approach to expenditure, particularly following the recall.
- R&D expenses of \$119.3 million increased 10%, reflecting the deliberate strategy to maintain momentum in the future development work of R&D.
- Net interest expense decreased \$3.3 million to \$4.3 million due to lower borrowings and lower unused line fees due to a reduction in the facility. Interest cover was 18 times (2011: 32 times).
- The tax rate of 21.3% fell by 2.1 percentage points. Excluding the impact of the product recall, the tax rate was 25.1%, up 1.7 percentage points. The change to the Australian R&D tax concession legislation effective 1 July 2011 led to a decrease in the benefit from the prior year of \$5.1 million (2.4 percentage points excluding the impact of the product recall).
- NPAT decreased 68% to \$56.8 million. Excluding the product recall costs, NPAT decreased 12% to \$158.1 million.

## Foreign exchange

- Foreign exchange was again an important aspect of the result.
- Cochlear has a partial natural hedge with over 90% of sales in foreign currency and over 50% of expenses in foreign currency. To help manage the portion not covered by the natural hedge, foreign exchange contracts on foreign currency cash flows back to Australia are taken out. These contracts cover a three year period at a declining level of cover.
- The Australian dollar strengthened again during the year against the USD and Euro, both hedged currencies.
- Foreign currency contracts applied against foreign cash inflows, resulted in a gain of \$74.4 million this year (2011: gain of \$77.4 million) recognised in revenue. This was in line with the movement in foreign currency rates according to our hedging policy.
- At 30 June 2012, Cochlear had foreign currency equivalent of \$509 million in foreign exchange contracts. In the coming year, F13, the average exchange rate for the US dollar contracts is 0.92 and the average for Euro contracts is 0.69.
- During the year, there was a net loss of \$0.3 million (2011: gain of \$2.5 million) on the translation of foreign assets. This is reported through Note 5 (Other income and other expenses) to the financial statements.
- Overall, NPAT was negatively impacted by \$23.7 million due to the movements in foreign exchange rates during the year.

## Increased dividends

- The final dividend of 125 cents per share brought the full year dividend to 245 cents per share. The full year dividend is up 9% on 2011.
- The final dividend is 35% franked, with 25% being Conduit Foreign Income.

## Strong capital management

### Strong cash generation

- Net cash provided by operating activities was \$168.3 million. There was net cash of \$2.9 million at 30 June 2012 (2011: \$9.4 million).
- The debt facility was increased by \$50 million to \$200 million, of which \$42 million was drawn as current and \$20 million drawn as non-current at 30 June 2012.
- Cochlear continues to meet all its debt covenant conditions.

### Debtors

- Debtor days decreased slightly to 73 days (2011: 74 days). Debtor days reduced in all regions as focus was made on cash collections.

### Inventories

- Inventories of \$101.3 million were down 5% (2011: \$106.1 million). Days inventory increased to 182 days (2011: 173 days), reflecting a build-up of finished goods inventory.

### Intangible assets

- Intangible assets of \$206.7 million (2011: \$208.6 million) are a significant proportion of Cochlear's total assets. Some \$151.1 million of this total relates to goodwill arising from the earlier acquisition of businesses.
- As a result of the recall, \$13.8 million of intangible assets were determined impaired and written down.
- All intangible assets are tested for impairment on an annual basis. There were no write-downs in 2012 other than the \$13.8 million related to the recall.

|                                                 | 2012<br>IFRS | 2011<br>IFRS | 2010<br>IFRS | 2009<br>IFRS | 2008<br>IFRS | 2007<br>IFRS | 2006<br>IFRS | 2005<br>IFRS | 2004<br>previous<br>GAAP | 2003<br>previous<br>GAAP |
|-------------------------------------------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------------------|--------------------------|
| Cochlear implant system sales (units)           | 23,087       | 24,661       | 21,023       | 18,553       | 18,228       | 15,947       | 12,901       | 10,802       | 9,306                    | 9,328                    |
| Total revenue (\$million)                       | 779.0        | 809.6        | 734.8        | 694.7        | 601.7        | 559.4        | 452.3        | 349.0        | 282.8                    | 306.1                    |
| R&D expenses (\$million)                        | 119.3        | 108.9        | 94.9         | 96.7         | 80.0         | 65.9         | 56.7         | 44.6         | 44.5                     | 37.0                     |
| NPAT (\$million)                                | 56.8         | 180.1        | 155.2        | 130.5        | 115.2        | 100.1        | 80.0         | 59.6         | 36.8                     | 58.2                     |
| EBITDA (\$million)*                             | 239.4        | 270.1        | 243.6        | 205.5        | 193.3        | 170.9        | 130.2        | 96.8         | 54.9                     | 87.9                     |
| EBIT (\$million)*                               | 215.3        | 242.7        | 220.5        | 183.3        | 167.3        | 150.2        | 111.5        | 82.5         | 45.5                     | 80.1                     |
| NPAT (\$million)*                               | 158.1        | 180.1        | 155.2        | 130.5        | 115.2        | 100.1        | 80.0         | 59.6         | 36.8                     | 58.2                     |
| Basic EPS (cents)                               | 100.0        | 318.2        | 275.7        | 233.7        | 208.1        | 182.9        | 146.8        | 110.1        | 68.2                     | 110.0                    |
| DPS (cents)                                     | 245.0        | 225.0        | 200.0        | 175.0        | 150.0        | 125.0        | 100.0        | 80.0         | 79.0                     | 77.0                     |
| Closing share price (\$)                        | 65.84        | 72.00        | 74.32        | 57.70        | 43.65        | 61.00        | 54.63        | 39.20        | 22.72                    | 32.30                    |
| Market capitalisation as at 30 June (\$million) | 3,744        | 4,081        | 4,198        | 3,230        | 2,423        | 3,341        | 2,985        | 2,123        | 1,231                    | 1,714                    |
| Number of employees                             | 2,390        | 2,319        | 2,006        | 1,888        | 1,789        | 1,655        | 1,100        | 982          | 816                      | 814                      |

\* Excludes product recall expenses of \$138.8 million before tax and \$101.3 million after tax in 2012

The following non-IFRS financial measures are included in this document:

- Excluding recall costs
- Constant currency
- Free cash flow.

Refer to page 105 for a discussion of these items.

# Cochlear continues to build its capabilities with a global team of approximately 2,500 people, based in 25 countries.

Of these, approximately 500 are engineers from a range of technical fields, supporting both development and manufacturing activities.

## Attracting and keeping the best people

In a competitive global talent market, Cochlear continues to maintain staff retention levels above the medical device industry average, with annualised voluntary turnover at 8.7% in F12.

As Cochlear grows, there is an increasing emphasis on internal career development for employees. During F12, Cochlear further developed programs to encourage internal career movement for employees, doubling the positions filled by internal candidates to 15%. Cochlear maintained its commitment to developing a strong talent pipeline, building our Graduate Engineering Program and Summer Internship Program, from which the very best graduates are attracted to Cochlear. These graduates participate in a broad development program as they rotate throughout the various aspects of Cochlear's business.

## Ongoing learning

To support individuals and to enhance team capability development, Cochlear continues to invest in employee learning and training development programs. Cochlear's Learning Management development system, Cochlear Academy, is deployed globally and provides employees with a range of flexible and multi-lingual learning options, modules, documents and webinars. There are now approximately 400 online learning modules on topics ranging from workplace health and safety, quality compliance to Cochlear products.

## Diversity

As a global company selling into over 100 countries, diversity is strongly encouraged at Cochlear and over 60 ethnic groups are represented in the Company's Sydney offices alone. This diversity is important in gaining a global understanding of the industry's complex issues.

Another area of emphasis is the advancement of female employees. Globally, 35% of our senior executive positions and 48% of employees are now women. Importantly, the proportion of female executive managers at Cochlear (22%) is higher than for other top 200 ASX organisations (which average 11%).

During F12, Cochlear maintained active programs to promote diversity in our workforce. This was recognised by winning the Australian HR Award for our work in promoting diversity. In addition, Cochlear continues to support the Women in Leadership

network, aimed at fostering the development of female leaders at Cochlear. Our Leadership Presence program for high performing female specialists has enabled women in Cochlear to grow their careers and was recognised by the Corporate Leadership Council as global best practice in promoting diversity.

## Ensuring the health and safety of employees

Cochlear remains committed to providing a healthy and safe workplace for all employees. Our workplace health and safety team has been active in promoting wellness programs and improved safety reporting, which has led to a reduction in the amount of accident related lost time and to improved safety investigation and auditing.

## Supporting the community

The Cochlear Foundation, established in 2007, continues its activities. The Foundation supports various programs promoting research and awareness of treatments for people with significant hearing impairment.

Cochlear supports community fundraising and corporate sporting activities, both financially and through direct involvement by employees.

Cochlear supports its employees' participation in community fundraising activities and corporate sporting activities. Among the events that Cochlear and its employees supported this year were the City2Surf Fun Run, the Sydney to Gong Bike Ride, the BRW Corporate Triathlon and Australia's Biggest Morning Tea.

In Europe, community activities were supported in several countries in F12 through team involvement and financial support. These include a range of different charities, mostly focused on helping the hearing impaired.

## Environmental responsibility

Cochlear supports a group of employees called "greenFEVER" whose goals are to raise awareness of environmental issues, promote sustainable living at work and at home, and identify possible activities to further reduce the Company's environmental impact. The group has been active in promoting alternative transport options and sharing energy saving ideas with employees.

Currently, Cochlear's emissions levels are significantly below the compulsory greenhouse gas reporting thresholds set out in the Energy Efficiency Opportunities program.

# Cochlear continues to focus on technologic innovation, a key growth driver

Cochlear's investment in research and development (R&D) remains a source of competitive advantage for the Company. In F12, Cochlear invested \$119.3 million, representing 15.3% of revenue, in its R&D activities.

Approximately 350 specialists from a range of engineering technology disciplines and backgrounds worldwide, make up Cochlear's design and development department. These highly specialised teams are based in Australia, Sweden, Belgium and the United States, and work together with over 100 external research partners based in 20 countries.

Focused technology groups continue work to improve hearing performance outcomes for recipients. Research spans basic scientific research, new technology developments and new product developments. This includes work on Cochlear's unique Dual-Microphone and input processing technologies, totally implantable cochlear implants, simplification through automation and wireless connectivity.

In F12, R&D continued work on advancing the Company's three in-market product lines: the Cochlear Nucleus range of cochlear implant systems, the Cochlear Baha range of bone conduction systems and the Cochlear Hybrid electro-acoustic hearing solution.

Clinical trials in Europe continue to show very encouraging results for the Company's fourth product line: the Cochlear Codacs range of direct acoustic cochlear implant systems.

In F12, Cochlear launched the Nucleus CI422 cochlear implant with Slim Straight electrode, the thinnest full length electrode on the market and an important addition to the Company's market leading electrode portfolio. The new Slim Straight electrode, which is specifically designed to help preserve cochlear structures and therefore residual hearing in recipients, has been approved by the FDA in America and the TUV in Europe.

A significant level of detailed investigation into the root cause of the CI500 series implant failure was also conducted in F12. In addition, further development work into the CI500 series implant was conducted and is ongoing to support the reintroduction of the product to market.

## Manufacturing operations

The manufacturing operations at Cochlear, located in Australia and Sweden, continue to allow the Company to deliver products of the highest quality and reliability.

Cochlear's manufacturing strategy is to ensure that production methods and capacity meet the ongoing reliability requirements but are also simplified to allow for improved efficiencies. Cochlear continues to run an operations improvement program, which incorporates "lean manufacturing" principles, and with ongoing investment in new manufacturing technologies which support flexibility and productivity improvements. In F12, this was demonstrated when production of Nucleus CI24RE implants was rapidly scaled up following the voluntary recall of Nucleus CI500 series implants.

Approximately 800 people are currently employed across Cochlear's manufacturing facilities.

## Quality assurance

Cochlear has a worldwide quality assurance system in place to ensure the quality of its products and services. This system complies with all applicable regulatory requirements around the world.

## Device approvals

Prior to commercial release, all medical devices must be approved by the relevant regulatory authorities. At present, Cochlear has all the necessary licences and approvals to enable the marketing of our products in the jurisdictions in which we operate. Ongoing approvals are regularly being sought for new products in a variety of jurisdictions.

Cochlear has recently been notified by a number of Regulatory Authorities, including TGA, FDA and European Competent Authorities that all necessary actions associated with the recall have been completed and the recall is now considered closed. The CI500 series implant will be submitted for reapproval as soon as the ongoing redesign and revalidation work is complete.

## Intellectual property

The creation of new intellectual property and the protection of that as well as our existing intellectual property remain key strategic imperatives for the business. In F12, Cochlear filed many new patent applications and currently holds more than 950 patents and patent applications globally.

# Cochlear's presence expanded in Latin America through its Panama based subsidiary

## Performance

- Revenue in the Americas region declined 2% in constant currency to \$297 million in large part due to the voluntary recall of the Nucleus CI500 series implant in September 2011.
- Upgrade revenue continued to increase as recipients took advantage of the Nucleus CP810 Sound Processor.

## Launches

- In June this year, after a successful controlled market release, Cochlear launched the Nucleus CI422 implant with Slim Straight electrode in the Americas region. Market feedback has been extremely positive.
- Cochlear significantly expanded its customer base in F12 with the Cochlear Baha 3 System. The Baha BI300 implant is the platform for future technology expansion and positions the Americas region well for growth.
- Cochlear continued to invest in recipient services and support including:
  - new recipient options were launched in F12 including 24/7 education, rehabilitation, new support web pages with video assets, electronic newsletters, applications for iPhone and Android devices and self-service tools; and
  - enhancements continue to improve the online recipient store, which is rapidly growing, now accounting for approximately 30% of all recipient orders.
- A new concierge program was launched connecting candidates with a team of audiologists to support and help the candidates in their decision-making.

## Emerging market footprint

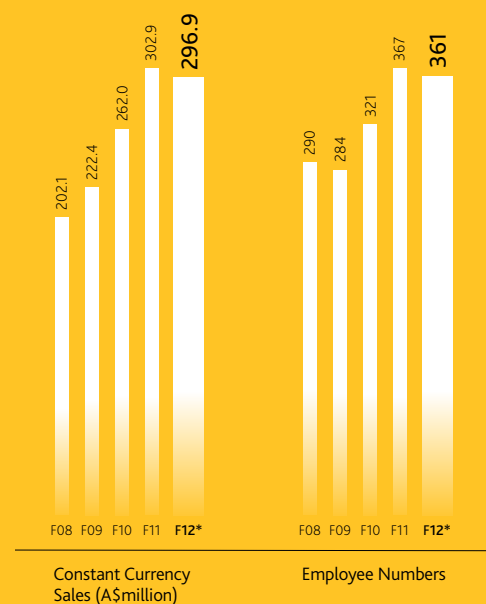
- Cochlear's presence expanded in Latin America through its Panama based subsidiary which serves 18 countries in Central America, South America and the Caribbean.

## Market growth

- In F12, Cochlear worked to expand clinical indications for the Nucleus system through the initiation of several clinical market research studies.
- Cochlear's growth strategy in the Americas region includes raising awareness of the technology and benefits of Cochlear solutions. In F12, the region expanded its consumer outreach program in 32 cities in the United States specifically targeting adults, the fastest growing population with hearing loss. This integrated program leveraged public relations, advertising, direct mail and educational events, providing an informative approach to awareness.
- The Cochlear Awareness Network continues to grow and provide support to both our current recipient base as well as to the regional awareness initiatives at the grass roots level.



## Americas Region



\* Financial years.

# Revenue in the EMEA region increased 2% in constant currency to \$285 million

Performance

- The EMEA region includes Europe, the Middle East and Africa.
- Revenue in the EMEA region increased 2% in constant currency to \$285 million.
- Nucleus cochlear implant technology continued to be well received following the recall of the CI500 series implant. Sales were quickly substituted for other Nucleus implants across the region. Upgrade revenue from Nucleus CP810 Sound Processors performed very well.

Launches

- The launch of Baha 3 Power Sound Processor was well received, continuing Cochlear's leadership in this important market segment.
- Cochlear launched its newest implant, the Nucleus CI422 implant with Slim Straight electrode, in EMEA in F12. This was the first region to launch the new implant, which is designed to preserve residual hearing. Early research work on the implant had originated in EMEA and the device rapidly gained market acceptance among surgeons.

Regional footprint

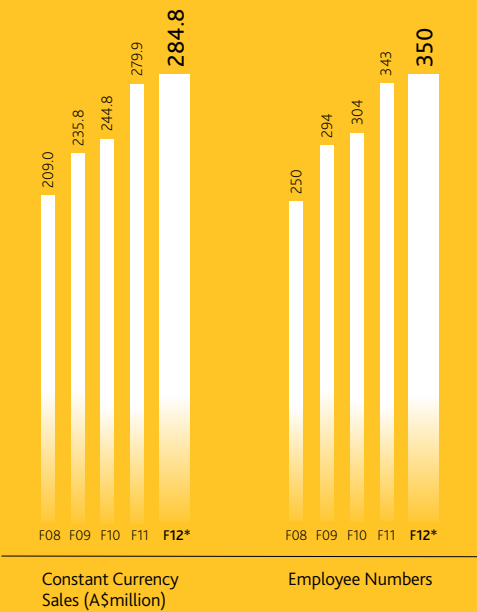
- Cochlear's online strategy is an important part of growing the market through improved awareness and access. In F12, a French online store was launched. It is designed to increase access for recipients to order spares and accessories more conveniently.
- A Cochlear website for healthcare professionals was launched, including an online newsletter, to ensure easy access to clinical and product information.
- A branch office in Prague (Czech Republic) was opened to service Cochlear's expanding presence in Central and Eastern Europe.

Market growth

- Cochlear continued to promote its products and showcase its technologies at a number of important industry events including the International Congress of Hearing Aid Acousticians (EUHA) in Nuremberg, Germany, the largest hearing technology congress in Europe.
- Leading healthcare professionals were brought together to discuss various clinical topics at Cochlear's 'Science and Research Seminars'. These included the first such seminar for public health bodies across the region to cover the increasingly significant topic of "Aging and Cochlear Implantation".
- A number of country-specific European Medical Advisory Board meetings were held with key EMEA opinion leaders who were to provide comment and direct input into Cochlear technologies and their applications. This is a crucial part of Cochlear's development process.



EMEA Region



\* Financial years.

# Revenue in the Asia Pacific region grew 4% in constant currency to a record \$123 million

## Performance

- Revenue in the Asia Pacific region grew 4% in constant currency to a record \$123 million.
- Growth was driven by strong overall results from Australia, Japan and India, supported by improved Nucleus sound processor sales.

## Driving growth in China and India

- China and India remained a focus in F12. The development of infrastructure is an important success factor in both markets and resources continued to be targeted at programs to advance surgery, audiology and rehabilitation expertise as well as after sales service.
- The private pay segment in China grew during F12 and showed strong surgery rates in the provincial clinics, with a transition from paediatric to adult recipients demonstrating the opportunity of this segment.
- In its second year of direct operations, Cochlear's business in India continued to refine its operational footprint and increase its competitiveness in the high growth market. A focus on education and the benefits of the premium Nucleus CP810 Sound Processor's Dual-Microphone technology proved a compelling proposition for upgrading.

## Upgrading to new technology

- Upgrades of sound processors were a focus for F12. Public policy in Australia improved, allowing the Australian Government to assist young adult recipients in the upgrade of sound processors up to the age of 26. Many Australian recipients took advantage of this opportunity.

## Executing strategy

- In F12, online projects to improve customer experience were launched including computerised recipient registration and product services. In Australia, an online store was launched, allowing customers to purchase items such as batteries and accessories over the internet.
- A policy unit was established to optimise reimbursement for both cochlear and bone conduction implants. New sources of funding were secured in China, India and Australia, with reimbursement now expected for Baha systems in both Korea and Japan in F13.
- Cochlear participated in the Asia Pacific Symposium on Cochlear Implant and Related Sciences, the region's biennial industry conference where the Company engaged with key industry leaders and demonstrated the benefits of Cochlear's unique Dual-Microphone technology.
- Three Research and Technology Labs were also held at Cochlear's Sydney headquarters to share and discuss new and future technologies with 70 of the region's key opinion leaders.



## Asia Pacific Region



\* Financial years.



#### 1. Mr Rick Holliday-Smith

Age 62. BA (Hons), FAICD, CA  
Appointed 1 March 2005

Director of Servcorp Limited since 1999. Director ASX Limited since 2006 and Chairman since March 2012. Chairman of Snowy Hydro Limited (not publicly listed) 2006 – 2012. Chairman of SFE Corporation Limited since 1999 until it merged with ASX Limited in 2006. Former director of St George Bank Limited (2007 – 2008), Exco Resources NL (1999 – 2006), DCA Group Limited (2004 – 2006) and MIA Group Limited (2000 – 2004). Former President of NationsBank-CRT, Chicago and Managing Director of Hong Kong Bank Limited, London.

Chairman of the Nomination Committee and Technology and Innovation Committee. Member of the Audit Committee and Human Resources Committee.

#### 2. Dr Chris G Roberts CEO/President

Age 58. BE (Hons), MBA, PhD, Hon DSc (Macq), FAICD, FTSE, FIEAust  
Appointed 1 February 2004

Chief Executive Officer/President of Cochlear Limited. Director of ResMed Inc since 1992 and Director of Research Australia (since 2003). Dr Roberts has worked in the medical device industry for more than 36 years in a number of senior management positions.

Member of the Medical Science Committee and Technology and Innovation Committee.

#### 3. Mr Paul R Bell

Age 66. BA, MA (Hons)  
Appointed 1 August 2005

Director of Biota Holdings Limited since 2006 and director of Westmead Medical Research. Former director of Bio-Link Partners Limited (2005 – 2009) and GroPep Limited (2003 – 2006). Extensive

executive career spanning 30 years with the international pharmaceutical company, Merck & Co Inc (Managing Director – Australia, 1988 – 1997; President of the Asia Pacific Human Health Division, 1997 – 2002).

Chairman of the Human Resources Committee. Member of the Nomination Committee and Technology and Innovation Committee.

#### 4. Prof Edward Byrne, AO

Age 60. DSc, MD, MBA, FRCP, FRACP  
Appointed 1 July 2002

Vice Chancellor of Monash University. Former director of Neurosciences Victoria Limited and UCL Hospital Group, London. Former executive Dean of the Faculty of Biomedical Sciences, Vice Provost and Head of the Medical School at University College, London. Former Dean of Faculty of Medicine, Nursing and Health Sciences at Monash University, Melbourne (2003 – 2006). Former director of Bupa Group Board, London, Neurosciences Australia Limited, the Baker Medical Research Institute, Burnet Medical Research Institute, Prince Henry's Medical Research Institute, Southern Health, and Mental Health Research Institute. Current director of Bupa Australia Pty Ltd.

Chairman of the Medical Science Committee. Member of the Nomination Committee and Technology and Innovation Committee.

#### 5. Mr Andrew Denver

Age 63. BSc (Hons) MBA, FAICD  
Appointed 1 February 2007

Chairman of Universal Biosensor Pty Limited since 2005 (director since 2002). Chairman of Speedx Pty Ltd since May 2009 and Principals Cornerstone Management Pty Limited (not publicly listed). Former Managing Director of Memtec Limited and President Asia for Pall Corporation.

Member of the Audit Committee, Human Resources Committee, Nomination Committee and Technology and Innovation Committee.

#### 6. Mr Donal P O'Dwyer

Age 59. BE Civil, MBA  
Appointed 1 August 2005

Chairman of Atcor Medical since 2004 and a director of Sunshine Heart Inc since 2004 and Mesoblast Limited since 2004. He also served as a director of Angioblast Systems Inc from 2005 through its acquisition in 2010. Former President of Cordis Cardiology (Johnson & Johnson medical device business unit) between 2000 and 2004.

Member of the Audit Committee, Human Resources Committee, Medical Science Committee, Nomination Committee and Technology and Innovation Committee.

#### 7. Mrs Yasmin Allen

Age 48. BCom, FAICD  
Appointed 2 August 2010

Director of Insurance Australia Group Limited (IAG) since 2004, member of IAG Audit, Risk Management and Compliance Committee and Chair of IAG Nomination, Remuneration and Sustainability Committee. Chair of Macquarie Specialised Asset Management (not publicly listed) since 2003. Director of the Australian Institute of Company Directors since 2010. Former non-executive director of Film Australia (2004 – 2008), Export Finance and Insurance Corporation (2001 – 2007) and Australian Red Cross Blood Service (2002 – 2005). Former Vice President of Deutsche Bank AG, Director of ANZ Investment Bank and Associate Director, HSBC London.

Chairman of the Audit Committee. Member of the Nomination Committee and Technology and Innovation Committee.



#### 1. Dr Chris Roberts – CEO/President

See “Board of Directors” on page 17.

#### 2. Richard Brook – President, European Region

BSc Management, MBA

Richard is responsible for the development and execution of the strategic direction for all our operations in Europe, Middle East and Africa. This includes sales in over 60 countries. Operations in Europe include sales, marketing, distribution, service, finance, regulatory and administration across this complex and diverse region.

Before joining Cochlear in 2003, Richard held senior roles in Guidant Corporation and Alaris Medical Systems. He has 19 years' experience in the medical device industry.

#### 3. Dr Bronwyn Evans – Senior Vice President, Global Quality, Clinical and Regulatory

BE (Hons), PhD, FIEAust

Bronwyn is responsible for ensuring the continued high quality of Cochlear's products together with coordinating the regulatory approval processes around the world for its products.

She joined the Company in 2005 after more than 20 years' experience in engineering and management roles in power generation and distribution, engineering education and the medical industry. Most recently, she worked as Asia Service Manager for GE Healthcare, Ultrasound based in Singapore. Bronwyn is a non-executive director of John Holland

Group, Chair of the Medical Technology Association of Australia (MTAA), Chair of the National Board of the Engineers Australia Centre for Learning and Management (CELM) and Chair of the Advisory Board for Robogals.

#### 4. Dig Howitt – Senior Vice President, Manufacturing and Logistics

BE (Hons), MBA

Dig is responsible for the development and execution of the strategic direction for the Cochlear supply chain. He and his team are responsible for the manufacture of all Cochlear products and all aspects of the supply chain, together with the introduction of new products from R&D into commercial production.

Prior to joining Cochlear in 2000, Dig had gained general management experience at Boral and Sunstate Cement, as well as being a consultant for Boston Consulting Group.

#### 5. Jan Janssen – Senior Vice President, Design and Development

MScEE

Jan leads a team of over 300 highly qualified engineers and scientists who implement the R&D strategy. This includes responsibility for identifying and developing cutting-edge technologies and commercial products.

Jan joined Cochlear in 2000 as head of the Cochlear Technology Centre based in Belgium, having previously worked with Philips Electronics where he was involved in R&D in the fields of high technology electronics and cochlear implants. Jan was

promoted to Senior Vice President, Design and Development in 2005.

#### 6. Michael Kavanagh – Senior Vice President, Global Marketing

BSc, MBA (Advanced)

Michael is responsible for the development of the global marketing strategy for Cochlear's product portfolio. This spans the identification of new product development opportunities through to product introduction and lifecycle management. This requires coordination and interpretation of research and then translating this into a relevant product portfolio together with marketing programs to drive disciplined growth.

Michael joined Cochlear in 2003, having held senior sales and marketing positions both locally and internationally in the pharmaceutical industry.

#### 7. Anne-Marie Leslie – Senior Vice President, Human Resources

BA (Hons), EMHRL

Anne-Marie joined Cochlear in February 2007 and is responsible for global human resources management. Her focus is on building people strategies to meet the demands of a fast growing, global company.

She has over 25 years' experience in local, regional and global human resource management roles, most recently with Bristol-Myers Squibb in the US. Earlier experience included quality management at Kodak as winners of the Australian Quality Prize and as an evaluator with Business Excellence Awards in Australia and the US.



**8. Neville Mitchell – Chief Financial Officer and Company Secretary**

BComm, CA (SA), CA

Neville is responsible for accounting, corporate finance, treasury and audit, together with investor relations, company secretarial and the corporate legal functions at Cochlear.

He joined the Company in 1990 and has been Chief Financial Officer since listing in 1995. Prior to joining Cochlear, he was a senior manager with KPMG in Johannesburg.

**9. David Morris – Chief Strategy Officer**

BBus, BAppSc

David is responsible for the development and execution of the global business strategy.

David was appointed as Chief Strategy Officer in 2011, having served as President, Cochlear Bone Anchored Solutions since 2005. He joined the Company in 2002 as Senior Vice President, Business Development.

Prior to joining Cochlear, he worked with Accenture in strategy and operational consulting, and has extensive international and Australian experience in the healthcare, consumer products, utilities and financial services industries.

**10. Prof Jim Patrick – Senior Vice President, Chief Scientist**

DEng, MSc

Jim is responsible for the global research portfolio of projects that feed into the commercial development stream. One of the original researchers involved with the cochlear implant program in Melbourne from 1975, Jim has worked in a number of senior managerial positions at Cochlear since its inception in 1981. Jim is an Associate Professor at the Department of Otolaryngology at The University of Melbourne and Adjunct Professor at La Trobe University.

**11. Mark Salmon – President, Asia Pacific Region**

MBA (Executive)

Mark is responsible for the development and execution of the strategic direction for all our operations in Australia, Asia and the South Pacific. This high potential region has complex regulatory sales and marketing drivers which require coordination of sales, marketing, third party distribution, regulatory and clinical infrastructure development activities. Mark also has global responsibility for Cochlear's information technology strategy and systems.

He joined Cochlear in 2004, after more than 20 years' experience in the medical industry, most recently as President and CEO of Asia Growth Markets and Australia, New Zealand and South East Asia for GE Medical Systems.

**12. Chris Smith – President, Americas Region**

BSc

Chris is responsible for the development and execution of the strategic direction for our operations in the Americas region, comprising North America, Central America and South America. Operations in the Americas include sales, marketing, distribution, service, finance, regulatory and administration across this fast growing region.

In September 2011, responsibility for Cochlear Bone Anchored Solutions was transferred to Chris in addition to his existing responsibilities.

He joined Cochlear in 2004, after more than 20 years' experience in the medical device industry specifically and healthcare in general in the US including Warburg Pincus, and as Group President for Gyrus Group (ENT and Surgical divisions).

Cochlear is committed to ensuring that its policies and practices reflect good corporate governance and that there is compliance with all corporate governance requirements applicable to Australian listed companies.

In this Corporate Governance Report, Cochlear sets out the key governance principles and practices of Cochlear and reports against the ASX Corporate Governance Council's Corporate Governance Principles and Recommendations with 2010 Amendments 2nd Edition (August 2007) (Guidelines). A checklist of the recommendations made in the Guidelines is set out at the end of this report. References to recommendations in the Guidelines are made throughout this report in order to indicate how Cochlear complies with the recommendations. All policies and terms of reference referred to in this report are published on the Company's website [www.cochlear.com](http://www.cochlear.com) in the Corporate Governance section, unless stated otherwise. The Corporate Governance section is located under the Investor Relations tab on the Company's website. Cochlear's corporate governance policies and procedures are reviewed on a regular basis and updated where appropriate.

#### **Principle 1: Lay solid foundations for management and oversight**

The Board of directors is responsible to Cochlear's shareholders and other stakeholders for the Company's overall business performance. The Board operates under a Board Charter that details its functions and the matters specifically reserved to it for decision (Rec 1.1). The charter is published in the Corporate Governance section of the Cochlear website (Rec 1.3). The Board is responsible for adopting Cochlear's business strategies and for monitoring management's implementation of those strategies. The Board considers and sets the Company's goals and performance targets, appoints and removes the CEO/President, oversees succession plans and approves the accounts, budgets, Risk Management Policy (including internal control and compliance), Code of Business Conduct and major capital management and expenditure decisions.

There is a clear distinction between the role and responsibilities of the Board and the role and responsibilities of the CEO/President (Rec 1.1). The balance of responsibilities between the Board and the CEO/President is reviewed on a regular basis so as to ensure that the division of functions remains appropriate to the needs of the Company.

The Chairman is responsible for leading the Board in the performance of its duties. The Board's prime objectives are to improve shareholder returns and to achieve disciplined and sustainable growth. The full Board meets for at least eight scheduled meetings each year. Other meetings are called as and when necessary. A summary of meeting attendance (including committee meeting attendance) for F12 is set out in the Directors' Report at page 29 (Recs 2.6, 4.4 and 8.4). At each Board meeting, the non-executive directors meet for a period without management or any executive directors present (Rec 2.1). Throughout the year, the Board has regular scheduled discussions on various aspects of the Company's strategy.

The CEO/President is responsible for the efficient and effective operation of Cochlear on a day-to-day basis. The CEO/President oversees the implementation of the strategies approved by the Board and is accountable to the Board for all authority delegated to the senior executive team. Notwithstanding these delegations by the Board, the CEO/President must consult the Chairman on matters that are sensitive, extraordinary or of a strategic nature. The CEO/President must bring all material matters to the Board's attention. The senior

executive team briefs the Board regularly so as to keep the Board up to date and to assist the directors with monitoring the results of operations. Each month, directors receive operating reports prepared by senior management, covering each region and function. Directors also regularly visit and inspect operations in Australia and overseas.

The performance of senior executives is evaluated in accordance with the Performance Evaluation Process Overview. The Performance Evaluation Process Overview is published in the Corporate Governance section of the Cochlear website (Rec 1.2). All employees, including senior executives, participate in biannual performance reviews, where achievement of key goals is discussed and assessed and future goals are agreed upon. A performance evaluation for senior executives took place in the reporting period and was carried out in accordance with the process disclosed (Rec 1.3).

#### **Principle 2: Structure the board to add value**

##### *Composition of the Board*

As at 30 June 2012, the Board comprised six non-executive directors (including the Chairman) and one executive director, the CEO/President. The Board is looking for directors to bring to the Board a mix of scientific, medical, technical and financial expertise as well as international business experience. The directors consider that, between them, they possess the necessary skills, knowledge and experience to allow the Board to perform its duties appropriately. Summaries of the relevant skills, experience and expertise of each director are set out on page 17 (Rec 2.6).

The policy for appointment of directors and the selection process are outlined in the Nomination Committee Terms of Reference, which are published in the Corporate Governance section of the Cochlear website (Rec 2.6). The Nomination Committee assesses the necessary and desirable competencies of candidates for directorship. The selection process includes obtaining advice from an external consultant to assist in identifying suitable candidates who meet the required specifications. Upon appointment of a new director, the key terms and conditions and the Company's expectations of the appointee are set out in a letter to the new director. The Nomination Committee actively considers gender diversity in carrying out its role. For further information on Cochlear's Diversity Policy, please see Principle 3: Promote ethical and responsible decision-making, below.

New non-executive directors are provided with an induction program specifically tailored to the needs of individual appointees. That program includes product training, one-on-one meetings with members of the senior executive team and visits to key functional areas. Directors participate in continuous improvement and education programs from time to time, as considered appropriate. The Company's Constitution requires one third of the directors to retire from office at the AGM each year. Retiring directors are eligible for re-election. The CEO/President is excluded from this requirement. Prof Edward Byrne, AO and Mr Andrew Denver will retire at the 2012 AGM and will stand for re-election at that meeting. A review of the performance of the Board, its committees and individual directors is performed at least every two years in accordance with the Performance Evaluation Process. The most recent review is being undertaken in 2012. The Chairman Mr Rick Holliday-Smith undertook individual interviews and questionnaires and subsequently held evaluations with each individual director as to their performance over the past year. The key findings of these reviews will be discussed at the Nomination Committee meeting held in October 2012. The Performance Evaluation Process

Overview gives details of performance evaluation for the Board, its committees and individual directors (Rec 2.5). The Performance Evaluation Process Overview is published in the Corporate Governance section of the Cochlear website.

The Chairman Mr Rick Holliday-Smith is an independent non-executive director (Rec 2.2). Mr Rick Holliday-Smith is not and has not previously been the CEO of the Company (Rec 2.3). Details of the division of responsibility between the Chairman and the CEO/President are set out above under Principle 1: Lay solid foundations for management and oversight (Rec 2.6).

#### *Independence*

The Board has assessed the independence of the non-executive directors in light of their interests and relationships and considers that all of the non-executive directors are independent (Rec 2.1). With the exception of the CEO/President, all directors on the Board are independent directors (Rec 2.1). An independent director is a non-executive director who is not a member of management and who is free of any business or other relationship that could materially interfere with, or could reasonably be perceived to materially interfere with, the independent exercise of their judgement. The Nomination Committee Terms of Reference outline the criteria used to determine the independence of the directors (Rec 2.6). The criteria used follow the criteria set out in the Guidelines.

Each year, the Board assesses the independence of the non-executive directors in light of the interests and circumstances disclosed by them. Independence is reassessed in the event of any material change of interests and circumstances. Any loss of independence by a non-executive director will immediately be disclosed to the market.

None of the non-executive directors has any business relationship with Cochlear. The total number of shares in the Company owned by non-executive directors is 21,770. This is considered immaterial.

The Board believes arbitrary limits on tenure may cause loss of experience and expertise that are important contributors to the efficient working of the Board. The Board does not currently believe that any non-executive directors have served on the Board for a period that could materially interfere with, or could reasonably be perceived to materially interfere with, the independent exercise of the relevant director's judgement. The period of office of each director is disclosed at page 17 (Rec 2.6). Currently, no director has served longer than 11 years on the Board. The longest serving director is Prof Edward Byrne, AO, who was appointed in 2002.

With the consent of the Chairman, individual directors may seek independent professional advice, at the expense of Cochlear, on any matter connected with their responsibilities (Rec 2.6). No individual directors exercised this right during the year.

#### *Board committees*

The Board has established five permanent committees to assist in the execution of its responsibilities. Each such committee reports to the Board. Each committee has terms of reference under which authority is delegated to it from the Board. The terms of reference for each committee can be viewed in the Corporate Governance section of the Cochlear website.

Committee meeting agendas, papers and minutes are made available to all members of the Board. The Chair of each committee is free to use whatever resources they consider necessary to discharge the committee's responsibilities. The number of committee meetings held during the year and the attendance at these meetings by

members are set out in the Directors' Report at page 29 (Recs 2.6, 4.4 and 8.4). With the exception of the Medical Science Committee and the Technology and Innovation Committee, all members of the committees are independent non-executive directors. Executive director Dr Chris Roberts is a member of the Medical Science Committee and the Technology and Innovation Committee.

The composition and role of each committee are set out below:

#### *Audit Committee (Rec 4.1)*

The Audit Committee meets at least four times a year. The Audit Committee consists entirely of independent non-executive directors (Rec 4.2). As at 30 June 2012, Mrs Yasmin Allen chaired the Committee, with the other members being the Chairman of the Board Mr Rick Holliday-Smith, Mr Andrew Denver and Mr Donal O'Dwyer (Recs 4.2 and 4.4). The Board considers that the Audit Committee is of a sufficient size and independence and possesses sufficient technical expertise to discharge its mandate effectively. An assessment of the technical expertise of the Committee's members occurs on an annual basis. The external and internal auditors, the CEO/President and the Chief Financial Officer (CFO) and other executives are invited to the meetings at the discretion of the Committee. At each Committee meeting they attend, the external auditor reports on the outcome of their audit and other work. The Committee meets with the external auditor in the absence of members of management at every meeting that the external auditor attends. Summaries of the Committee members' technical expertise are set out at page 17 (Rec 4.4). The Audit Committee Terms of Reference set out the Committee's role and responsibilities, composition, structure and membership requirements. The Audit Committee Terms of Reference can be viewed in the Corporate Governance section of the Cochlear website (Recs 4.3 and 4.4).

The principal role of the Audit Committee is to advise and assist the Board in relation to the reporting of financial information and management of risk and to assist the Board in:

- ensuring the Company adopts, maintains and applies appropriate accounting and reporting processes and procedures;
- facilitating the independence of the external audit process and addressing issues arising from the audit process; and
- ensuring the Company maintains effective risk management and internal control systems.

Cochlear's processes relating to financial reporting are outlined below at Principle 4: Safeguard integrity in financial reporting. Cochlear's processes relating to risk management and internal control are outlined below at Principle 7: Recognise and manage risk.

#### *Human Resources Committee*

The Human Resources Committee (which was formerly known as the Remuneration Committee) meets at least three times a year. As at 30 June 2012, Mr Paul Bell chaired the Committee, with the other members being the Chairman of the Board Mr Rick Holliday-Smith, Mr Andrew Denver and Mr Donal O'Dwyer. All members of the Human Resources Committee are independent non-executive directors (Rec 8.4). As the need arises, the CEO/President, CFO, Senior Vice President, Human Resources and other executives are invited to meetings at the discretion of the Committee.

The Human Resources Committee Terms of Reference set out the Committee's role and responsibilities, composition, structure and

membership requirements. The Human Resources Committee Terms of Reference can be viewed in the Corporate Governance section of the Cochlear website (Rec 8.4).

The Human Resources Committee's responsibilities include making recommendations to the Board in relation to the Remuneration Policy and the amounts and composition of remuneration for the CEO/President and other members of the senior executive team. This includes long-term performance requirements and incentives. Remuneration levels are set at competitive levels to attract and retain qualified and experienced staff. Independent advice is taken on the appropriateness of remuneration packages.

The Committee's role includes responsibility for the remuneration and incentive policies (including the Performance Appraisal Policy) for the Chairman and other non-executive directors as well as for Cochlear generally. The Committee also approves the recruitment, retention and termination policies and practices as well as superannuation arrangements and makes recommendations to the Board in accordance with the Cochlear Executive Long Term Incentive Plan (CELTIP). The Human Resources Committee's role includes responsibility for the Cochlear Diversity Policy including the implementation and monitoring of the policy. Further information on Cochlear's Diversity Policy can be found below at Principle 3: Promote ethical and responsible decision-making.

The Human Resources Committee is authorised to seek any information it requires from internal resources and to take independent professional advice as it considers necessary.

Further details on Cochlear's remuneration policies and the principles upon which they are based are set out below at Principle 8: Remunerate fairly and responsibly and in the Remuneration Report at pages 32 to 42 (Rec 8.4).

#### *Nomination Committee (Rec 2.4)*

The Nomination Committee is chaired by the Chairman of the Board Mr Rick Holliday-Smith and, as at 30 June 2012, the other members of the Committee were Mrs Yasmin Allen, Mr Paul Bell, Prof Edward Byrne, AO, Mr Andrew Denver and Mr Donal O'Dwyer (Rec 2.6). The Nomination Committee is comprised entirely of independent non-executive directors.

The Nomination Committee was established in July 2003. The Committee's role is to assist the directors in ensuring that the Board is comprised of individuals who are best able to discharge the responsibilities of a director. The Nomination Committee's role includes:

- annually assessing the skills, knowledge, experience, independence and diversity required on the Board and the extent to which each is represented and making recommendations to the Board;
- establishing processes for the review of the performance of individual directors and the Board as a whole;
- establishing processes for the identification of suitable candidates for appointment to the Board;
- reviewing skills required to be maintained by existing directors and recommending ways in which the skills of directors can be enhanced; and
- overseeing succession planning for the Board and the CEO/President.

The Nomination Committee Terms of Reference set out the Committee's role and responsibilities, composition, structure and membership requirements. The Nomination Committee Terms of Reference can be viewed in the Corporate Governance section of the Cochlear website (Rec 2.6). The Nomination Committee Terms of Reference include a description of the procedure for the selection and appointment of new directors and the criteria used to determine director independence (Rec 2.6).

As a part of the appointment process, prospective directors must disclose existing and proposed directorships as well as any other commitments they have. These commitments are assessed to determine whether the prospective director has adequate time to perform their duties. The Nomination Committee assesses the time commitments of the Chairman and all other non-executive directors on an ongoing basis so as to ensure that adequate time is available to discharge Board duties. The current members of the Board are all considered to have sufficient time available to them in order to discharge their responsibilities to Cochlear.

#### *Medical Science Committee*

The Medical Science Committee was established during the 2003 financial year. As at 30 June 2012, Prof Edward Byrne, AO chaired the Committee, with the other members being Mr Donal O'Dwyer and Dr Chris Roberts. The Committee may invite any Cochlear executive to attend its meetings at its discretion.

The Medical Science Committee Terms of Reference set out the Committee's role and responsibilities, composition, structure and membership requirements. The Terms of Reference provide for the Committee to meet on an "as needs" basis, but at least biannually. The Medical Science Committee Terms of Reference can be viewed in the Corporate Governance section of the Cochlear website.

The Medical Science Committee considers any matters relating to medical aspects of Cochlear's businesses and related technologies. This includes a watching brief on medical developments in these fields and the findings of independent medical experts. The Medical Science Committee has provided oversight and guidance in relation to the recall of the unimplanted Nucleus CI500 series implants. The Committee has met on a number of occasions since the recall and has closely monitored developments for quality and regulatory implications.

#### *Technology and Innovation Committee*

The Technology and Innovation Committee was established during the 2003 financial year. As at 30 June 2012, the Committee was chaired by the Chairman of the Board Mr Rick Holliday-Smith, with the other members being Mrs Yasmin Allen, Mr Paul Bell, Prof Edward Byrne, AO, Mr Andrew Denver, Mr Donal O'Dwyer and Dr Chris Roberts. Executives of the Company are invited to meetings at the discretion of the Committee.

The Technology and Innovation Committee Terms of Reference set out the Committee's role and responsibilities, composition, structure and membership requirements. The Technology and Innovation Committee Terms of Reference can be viewed in the Corporate Governance section of the Cochlear website. The Committee oversees the strategic direction of the Company's technology research and product development programs with an emphasis on priority and resource allocation in line with the Company's agreed corporate strategy.

### Principle 3: Promote ethical and responsible decision-making

#### Conduct

All Cochlear personnel, including the directors and the senior executive team, are expected to act with the utmost integrity and objectivity, striving at all times to enhance the reputation and performance of Cochlear. Cochlear's values are enunciated in the Code of Business Conduct and are reflected in Cochlear's mission statement and strategic plan (Rec 3.1). The Code guides the directors, the senior executive team and all employees as to:

- the practices which are necessary to maintain confidence in the Company's integrity;
- the practices necessary to take into account their legal obligations and the reasonable expectations of their stakeholders; and
- the responsibility and accountability of individuals for reporting and investigating reports of unethical practice.

The Code requires strict compliance with high standards of honesty, integrity and fairness in all conduct relating to Cochlear and its products. The Code outlines requirements relating to anti-corruption, confidentiality/privacy, trade practices, documentation management, workplace and other compliance issues for the purpose of ensuring that the Company meets best practice in these areas. The Code also provides for clear and confidential reporting mechanisms concerning any potential breach. The Company has a whistleblower policy to ensure that the confidentiality, investigation and reporting of any allegations relating to improper conduct are properly maintained. The whistleblower policy is an internal document and is not available on the Cochlear website.

The Code of Business Conduct can be viewed in the Corporate Governance section of the Cochlear website (Rec 3.5).

The Company has documented policies on equal opportunity, occupational health and safety and standards of workplace behaviour, which are communicated to employees at the time of employment. These policies are reinforced by continuous performance management and employee training programs. These policies are internal documents and are not available on the Cochlear website.

Directors and the senior executive team are subject to the Non-Executive Directors and Executives Share Ownership Policy. This Policy specifies minimum levels of shareholdings for directors and the senior executive team. The Non-Executive Directors and Executives Share Ownership Policy is an internal document and is not available on the Cochlear website.

All directors, senior executives and employees are subject to Cochlear's Trading Policy. Consistent with the Corporations Act 2001, directors, senior executives and employees are prohibited by the Trading Policy from dealing in the Company's securities whilst in possession of "inside information". Subject to certain limited exceptions, the Trading Policy prohibits "Designated Persons" (which includes the Company's key management personnel and certain other persons) from dealing in Cochlear securities outside of set trading windows. During the trading windows, Designated Persons must still seek "no objection" from the Company prior to trading in Cochlear securities. Employees who are not Designated Persons are not restricted to dealing within the trading windows. However, in order to mitigate the risk of inadvertently trading whilst in possession of inside information, the Policy advises employees to trade in the

Company's securities only during the trading windows. Employees are encouraged to seek advice from the Company Secretary prior to trading if they are in any doubt as to whether they are in possession of inside information.

Compliance with the Trading Policy is monitored. The Audit Committee receives a report at each of its meetings regarding trading in the Company's securities by the CEO/President and other members of the senior executive team. Share dealings by directors are promptly notified to the ASX in accordance with the ASX Listing Rules.

Executives who are granted shares under the CELTIP are provided with details of the Trading Policy and the trading windows as well as guidelines on what constitutes insider trading. The Trading Policy can be viewed in the Corporate Governance section of the Cochlear website.

#### Diversity

As a global business, Cochlear is committed to providing an inclusive workplace that attracts the best employees to support its growth business. Cochlear therefore needs people with a diverse range of skills, expertise and diversity in terms of gender, age and ethnicity. To this end, the focus of the Company's workforce demographics objectives is to continuously build organisational capabilities to achieve Cochlear's business vision and mission.

Cochlear's policy is to recruit and manage on the basis of competence and performance regardless of age, nationality, race, gender or cultural background. As a business founded on technology leadership, the Company places a particular focus on attracting and retaining staff with science, technology, engineering and mathematical skills to drive long-term value creation in the business.

To ensure the Company meets its ongoing commitment to diversity, Cochlear has established a Diversity Policy (Rec 3.2). The Diversity Policy can be viewed in the Corporate Governance section of the Cochlear website (Rec 3.5). The Diversity Policy sets out the following Workforce Objectives:

- growing the diversity of Cochlear's workforce to reflect the Company's business needs and the global community it serves;
- implementing programs that prepare women to take on senior roles within the business both in operational and specialist support areas;
- implementing programs to attract a diverse workforce; and
- investing in initiatives to enable Cochlear's People Managers to provide an inclusive working environment to retain staff.

These Workforce Objectives will each have annual initiatives which are approved and monitored by the Board's Human Resources Committee. These annual initiatives include initiatives with measurable objectives for achieving gender diversity (Rec 3.2). The outcomes of all annual initiatives are assessed as part of the annual workforce demographics review by the Board's Human Resources Committee (Rec 3.2). A summary of the F12 annual initiatives to implement Cochlear's Workforce Objectives, together with the progress achieved for each initiative, is set out below in Table 1 (Rec 3.3). Cochlear's gender profile, including the percentage of women employees in the whole organisation, women in senior executive positions and women on the Board, is set out below in Table 2 (Rec 3.4).

Table 1: F12 Annual Initiatives and Progress

| Workforce Objectives                                                          | Annual Initiative and Progress                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                           |
|-------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Growing the workforce to meet Cochlear's business needs in a global community | <p><b>Science Technology Engineering and Mathematics (STEM)</b><br/>As a technology company, Cochlear needs to attract and maintain key skills for innovation in STEM areas. 64% of senior employees at Cochlear (Band 1 and their direct reports in Australia) have a STEM qualification and need this in order to perform their role.</p> <p><b>Increase the representation of women in the workforce</b><br/>47% of Cochlear's total permanent full-time workforce is female. 34% of managerial roles (Bands 1–3) are filled by females. Presently, in Australia one third of new hires in executive roles and more than half of new hires in Senior Manager roles are female. In F12, 45.7% of new recruits were female.</p> <p>In F12, Cochlear recruited two female Senior Managers, four female Line Managers, four female Principal Specialists and 13 female Senior Specialists. These new hires increased the representation of females in all categories with the exception of the Principal Specialists, where the proportion of females remained stable. 31% of Cochlear's top and emerging talent are female and so, across key roles and pipelines, Cochlear is above the manufacturing industry average of 25.6% female. Cochlear's annualised voluntary turnover is 8.7% globally and 6.6% in Australia. These rates are very competitive for a medical device business.</p>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                            |
| Implementing programs that prepare women for senior roles                     | <p><b>Human capital planning for recruitment and development for executive roles</b><br/>During F12, females were appointed to two country manager roles and to two senior level support roles.</p> <p><b>Development programs</b><br/>Cochlear introduced a "Leadership Presence" program for high performing women during F12. Of 30 participants, 68% assumed greater business responsibility following completion of the program and 30% were promoted. The program has been selected as a global best practice by the Corporate Leadership Council.</p> <p><b>Women in Leadership network</b><br/>Support and sponsorship through the Women in Leadership network continued in F12 with external presenters, mentoring events and sponsorship for involvement in external networks.</p>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                             |
| Attracting diverse talent to meet Cochlear's business needs                   | <p><b>Promotion of science and engineering careers</b><br/>During F12, Cochlear has promoted science and engineering careers through its support of Engineering Australia, support and sponsorship for Robogals (an organisation committed to fostering female participation in science and engineering programs in schools) and participation in career programs for the University of Wollongong and Macquarie University.</p> <p><b>Building Cochlear's graduate pipeline</b><br/>Cochlear has continuously invested in graduate recruitment. Since 2006, Cochlear has operated a formal graduate development program to ensure the Company attracts the top talent from Australian universities so as to build a pipeline of people for product development, manufacturing and quality roles within the business. The Summer Internship Program during F12 attracted 342 applicants. Four females and 10 males were accepted into the program. The F12 Graduate Engineering Program attracted 14 applicants for six places. Two of these places were filled by female applicants.</p> <p><b>Promotion of Cochlear's Employee Value Proposition</b><br/>Cochlear was the winner of the 2011 Australian HR Award for "Best Employee Value Proposition". Of 254 staff recruited in F12, 45.7% were female. The Company received a 5% increase in applications when compared to the previous year. 24% of applications received in F12 were from females, and 39% of successful candidates were female. Overall, females represented a higher proportion of successful applicants (2.7% of female applicants were successful compared to 1.5% male applicants). During F12, Cochlear further developed programs to encourage internal career movement for employees. During F12, the percentage of positions filled internally increased to 15%, with one in 10 internal applications being successful. Men and women were equally represented in internal promotions and had the same success rate.</p> |
| Investing in people manager development                                       | <p><b>Leadership Development</b><br/>199 managers (136 People Managers and 63 Managers of Managers) are enrolled and completing self-directed learning in Cochlear's Learning Management development system. A total of 31 leadership development workshops were conducted during F12. During F12 the Company introduced a new leadership assessment and development approach and 20 People Managers completed the assessment.</p>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                       |

Table 2: Cochlear's workforce gender profile

| Workplace Profile               |                     | Cochlear Limited – 30 June 2012 |        |                     |      |        |                 |       |        |
|---------------------------------|---------------------|---------------------------------|--------|---------------------|------|--------|-----------------|-------|--------|
| Occupational Category           | Permanent Full-Time |                                 | %      | Permanent Part-Time |      | %      | Total Employees |       | %      |
|                                 | Female              | Male                            | Female | Female              | Male | Female | Female          | Male  | Female |
| Board (including CEO/President) | 1                   | 6                               | 14%    | 0                   | 0    | 0%     | 1               | 6     | 14%    |
| Senior Executive Positions      | 61                  | 128                             | 32%    | 8                   | 1    | 89%    | 69              | 129   | 35%    |
| Whole Organisation              | 1,071               | 1,220                           | 47%    | 83                  | 16   | 84%    | 1,154           | 1,236 | 48%    |

#### Principle 4: Safeguard integrity in financial reporting

The directors are committed to the preparation of financial statements that present a balanced and clear assessment of the Company's financial performance, position and prospects.

Accounting and financial control policies and procedures have been established and are monitored by the Audit Committee (Rec 4.1). The Committee approves any new material accounting policies. Compliance with these policies and procedures is subject to review by the external and internal auditors. The Committee provides a link between the external auditor and the Board and monitors compliance with statutory responsibilities. The Audit Committee is responsible for making recommendations on the appointment, evaluation and dismissal of the external auditor, setting fees and ensuring that the external auditor reports to the Committee and the Board (Rec 4.4). The Audit Committee reviews the performance, independence and objectives of the external auditor on an annual basis. Details relating to the selection and appointment of the Company's external auditor are included in the Audit Committee Terms of Reference (Rec 4.4).

Additional detail relating to the Audit Committee and the Audit Committee Terms of Reference can be found above at Principle 2: Structure the board to add value (Rec 4.4).

Cochlear is committed to auditor independence. The Cochlear audit engagement partner must rotate every five years, with the last rotation occurring in July 2011. The Audit Committee reviews the independence of the external auditor at each of its meetings. All non-audit services provided by the Company's external audit firm must be approved or ratified by the Audit Committee.

Cochlear has a highly structured six monthly reporting process, culminating in Board sign-off and release of financial results to the market. In accordance with section 295A of the Corporations Act 2001, the CEO/President and the CFO provide a written statement to the Board that the Company's published financial reports present a true and fair view, in all material respects, of the Company's financial condition and that the operational results are in accordance with relevant accounting standards.

#### Principle 5: Make timely and balanced disclosure

Cochlear is committed to effective communication with its investors so as to give them equal and timely access to accurate, balanced and understandable information.

Cochlear's Continuous Disclosure Policy and Procedures set out the Company's policies and procedures in relation to the disclosure of information (Rec 5.1). The Policy and Procedures aim to ensure full and timely disclosure to the market of all material issues relating to Cochlear and to ensure all stakeholders have an equal opportunity to access that information. The Policy and Procedures are designed to ensure that the disclosure requirements set out in the ASX Listing Rules and the Corporations Act 2001 are complied with and to ensure accountability at a senior management level for that compliance. The Policy and Procedures are reviewed on a regular basis.

The Continuous Disclosure Policy and Procedures can be viewed in the Corporate Governance section of the Company website (Rec 5.2)

#### Principle 6: Respect the rights of shareholders

The Board and senior executive team are committed to formulating and implementing Company strategy. The shareholders of the Company play a key role in the governance of the Company. The directors recognise that shareholders must receive timely information about the Company in order to play their role effectively. The directors appreciate that information communicated to shareholders needs to be of high quality, relevant, balanced and understandable. The Company's Shareholder Communications Policy is published in the Corporate Governance section of the Cochlear website (Recs 6.1 and 6.2). The Policy is designed to promote effective communications with shareholders and to encourage shareholders to participate in general meetings of the Company.

The principal channels of communication with the Company's shareholders are the provision of the half yearly and annual reports, periodic analyst and media briefings, the distribution of specific material covering major transactions and events, Company announcements and the AGM. Cochlear offers its shareholders the ability to receive distributed materials in either electronic or hard copy format.

The Board's philosophy is to encourage full participation of shareholders at the AGM to ensure a high level of accountability and identification with Cochlear's strategy and goals. The Company provides a forum to address individual shareholders' questions at each AGM. The external auditor attends the AGM and is available to answer questions about the conduct of the audit and the preparation and content of the Audit Report. In addition to attending the AGM in person, shareholders may view a webcast of the AGM online. Advance notice of the timing of half year and full year results announcements is provided on the Cochlear website. Copies of results presentations are made available via the Cochlear and ASX websites.

In addition, shareholders may at any time direct questions or requests for information to the Company Secretary, the CEO/President or the Chairman. Shareholders can also gain access to information about Cochlear, including annual reports, key policies and the Terms of Reference of its Board committees, through the Cochlear website.

#### Principle 7: Recognise and manage risk

Cochlear views risk management as integral to its objectives of effective management of Company assets and the creation and maintenance of shareholder value. The Board has established a Risk Management Policy. This Policy provides a framework for the oversight and management on a continuing basis of the material business risks associated with Cochlear's activities (Rec 7.1). Cochlear assesses its risk management framework against the International Standard for Risk Management ISO 31000. The Risk Register puts the Risk Management Policy into effect. The Risk Register was designed and is implemented so as to provide a comprehensive risk management system which identifies, assesses and appropriately manages Cochlear's material business risks (Rec 7.2). Cochlear focuses on effective management of material business, operational, financial, human resources and legal risks. Within these categories, specific identified risks arise from matters such as actions by competitors, technological developments, government policy changes and exchange rate movements.

The Board, Audit Committee and senior executive team are together accountable for monitoring risk and implementing the Risk Management Policy. The Board oversees implementation of the Risk Management Policy and the Risk Register. The Board ensures that investors are informed of material changes to the Company's risk profile.

The Audit Committee advises the Board and reports on the status of major risks to the Company through the integrated risk management programs. Day-to-day management of the Risk Register is delegated to the Risk Management Committee. The Risk Management Committee is made up of senior executives.

The Risk Management Committee reports on the effectiveness of the Company's management of its material business risks at each Audit Committee meeting, including minutes of all Risk Management Committee meetings (Rec 7.2). The Risk Management Committee is responsible for identification of areas of risk, prioritisation of these risks and adoption of cost effective strategies, where appropriate, to manage Cochlear's exposure. Senior executives charged with the responsibility for identifying and managing these risks are required to sign off on them on a quarterly basis. The Risk Management Committee has reported to the Board on the effectiveness of the Company's management of business risks (Recs 7.2 and 7.4).

The Audit Committee advises the Board on risk management and is responsible for reviewing the effectiveness of Cochlear's approach to risk management and the establishment and maintenance of internal compliance and control systems within the risk management framework. This includes the scope of the Internal Audit function. The Audit Committee is responsible for the appointment and removal of the internal auditor and for ensuring that the internal auditor is independent from the external auditor.

Whilst particular internal audit programs may be outsourced, the internal and external audit functions are separate and independent of each other. The Audit Committee approves the internal audit program for each year and the effectiveness of the function is kept under review. All reports issued by the internal auditor are tabled at Audit Committee meetings.

The Board has received assurance from the CEO/President and the CFO that the declarations provided by each of the CEO/President and CFO in accordance with section 295A of the Corporations Act 2001, regarding the integrity of the financial statements, are founded on a sound system of risk management and internal control and that the system is operating effectively in all material respects in relation to financial reporting risks (Rec 7.3). The Risk Management Policy can be viewed at the Corporate Governance section of the Cochlear website (Rec 7.4).

#### **Principle 8: Remunerate fairly and responsibly**

The Board has established the Human Resources Committee to focus on appropriate remuneration policies which are designed to enhance corporate and individual performance (Rec 8.1). The Human Resources Committee Terms of Reference are published in the Corporate Governance section of the Cochlear website. These Terms of Reference set out the Human Resources Committee's role and responsibilities, composition, structure and membership requirements (Rec 8.4).

Further detail relating to the Human Resources Committee, including a signpost to the record of attendance at its meetings, can be found above at Principle 2: Structure the board to add value (Rec 8.4).

Cochlear's Remuneration Policy and practices are designed to attract, motivate and retain high quality people.

The Remuneration Policy is built around principles that:

- remuneration be linked to Cochlear's performance and the creation of shareholder value;
- directors' remuneration be competitive and reflect good corporate governance;
- executive and employee rewards be competitive in the markets in which Cochlear operates;
- executive and relevant employee remuneration be an appropriate balance of fixed and variable reward;
- variable remuneration for senior management be comprised of short and long-term components; and
- a significant proportion of executive and employee reward be dependent upon performance assessed against key business measures, both financial and non-financial.

Details of F12 remuneration (including retirement benefits) of the directors and specified executives are included in the Remuneration Report on pages 32 to 42. Further disclosure in relation to the remuneration philosophy is included in the Remuneration Report.

#### *Non-executive directors' remuneration policy*

Fees for non-executive directors are based on the nature of their work and their responsibilities. In determining levels of fees, survey data on comparable companies is considered. Non-executive directors' fees are recommended by the Committee and determined by the Board within the aggregate amount approved by shareholders at the 2011 AGM of \$2,000,000 a year.

The structure of non-executive directors' remuneration is clearly distinguished from that of executive directors and senior executives (Rec 8.3). Non-executive directors do not receive any options, performance shares or other performance related remuneration. All non-executive directors receive the statutory superannuation awards only. Any amounts due under the closed directors' retirement scheme have been frozen and are indexed by reference to the bank bill rate (Rec 8.4).

#### *Senior executives' remuneration policy*

Remuneration for Cochlear executives includes both fixed and variable incentive components. Equity based executive remuneration is made in accordance with the CELTIP. The CELTIP was approved by shareholders at the 2003 AGM. The exercise periods for the CELTIP are timed to coincide with the trading windows provided in the Company's Trading Policy. In line with the Corporations Act 2001, the Trading Policy prohibits executives from hedging unvested CELTIP awards (Rec 8.4).

## ASX Corporate Governance Council's Corporate Governance Principles and Recommendations checklist

| Number      | Requirement                                                                                                                                                                                                                                                                                                                                                                                                                                                                                          | Compliant |
|-------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------|
| <b>Pr 1</b> | <b>Lay solid foundations for management and oversight</b>                                                                                                                                                                                                                                                                                                                                                                                                                                            |           |
| Rec 1.1     | Companies should establish the functions reserved to the board and those delegated to senior executives and disclose those functions.                                                                                                                                                                                                                                                                                                                                                                | ✓         |
| Rec 1.2     | Companies should disclose the process for evaluating the performance of senior executives.                                                                                                                                                                                                                                                                                                                                                                                                           | ✓         |
| Rec 1.3     | Companies should provide the information indicated in the Guide to reporting on Principle 1.                                                                                                                                                                                                                                                                                                                                                                                                         | ✓         |
| <b>Pr 2</b> | <b>Structure the board to add value</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                              |           |
| Rec 2.1     | A majority of the board should be independent directors.                                                                                                                                                                                                                                                                                                                                                                                                                                             | ✓         |
| Rec 2.2     | The chairman should be an independent director.                                                                                                                                                                                                                                                                                                                                                                                                                                                      | ✓         |
| Rec 2.3     | The roles of chairman and chief executive officer should not be exercised by the same individual.                                                                                                                                                                                                                                                                                                                                                                                                    | ✓         |
| Rec 2.4     | The board should establish a nomination committee.                                                                                                                                                                                                                                                                                                                                                                                                                                                   | ✓         |
| Rec 2.5     | Companies should disclose the process for evaluating the performance of the board, its committees and individual directors.                                                                                                                                                                                                                                                                                                                                                                          | ✓         |
| Rec 2.6     | Companies should provide the information indicated in the Guide to reporting on Principle 2.                                                                                                                                                                                                                                                                                                                                                                                                         | ✓         |
| <b>Pr 3</b> | <b>Promote ethical and responsible decision-making</b>                                                                                                                                                                                                                                                                                                                                                                                                                                               |           |
| Rec 3.1     | Companies should establish a code of conduct and disclose the code or a summary of the code as to: <ul style="list-style-type: none"> <li>the practices necessary to maintain confidence in the company's integrity;</li> <li>the practices necessary to take account of their legal obligations and the reasonable expectations of their stakeholders; and</li> <li>the responsibility and accountability of individuals for reporting and investigating reports of unethical practices.</li> </ul> | ✓         |
| Rec 3.2     | Companies should establish a policy concerning diversity and disclose the policy or a summary of that policy. The policy should include requirements for the board to establish measurable objectives for achieving gender diversity for the board to assess annually both the objectives and progress in achieving them.                                                                                                                                                                            | ✓         |
| Rec 3.3     | Companies should disclose in each annual report the measurable objectives for achieving gender diversity set by the board in accordance with the diversity policy and progress towards achieving them.                                                                                                                                                                                                                                                                                               | ✓         |
| Rec 3.4     | Companies should disclose in each annual report the proportion of women employees in the whole organisation, women in senior executive positions and women on the board.                                                                                                                                                                                                                                                                                                                             | ✓         |
| Rec 3.5     | Companies should provide the information indicated in the Guide to reporting on Principle 3.                                                                                                                                                                                                                                                                                                                                                                                                         | ✓         |
| <b>Pr 4</b> | <b>Safeguard integrity in financial reporting</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                    |           |
| Rec 4.1     | The board should establish an audit committee.                                                                                                                                                                                                                                                                                                                                                                                                                                                       | ✓         |
| Rec 4.2     | The audit committee should be structured so that it: <ul style="list-style-type: none"> <li>consists only of non-executive directors;</li> <li>consists of a majority of independent directors;</li> <li>is chaired by an independent chair, who is not chair of the board; and</li> <li>has at least three members.</li> </ul>                                                                                                                                                                      | ✓         |
| Rec 4.3     | The audit committee should have a formal charter.                                                                                                                                                                                                                                                                                                                                                                                                                                                    | ✓         |
| Rec 4.4     | Companies should provide the information indicated in the Guide to reporting on Principle 4.                                                                                                                                                                                                                                                                                                                                                                                                         | ✓         |
| <b>Pr 5</b> | <b>Make timely and balanced disclosure</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                           |           |
| Rec 5.1     | Companies should establish written policies designed to ensure compliance with ASX Listing Rule disclosure requirements and to ensure accountability at a senior executive level for that compliance and disclose those policies or a summary of those policies.                                                                                                                                                                                                                                     | ✓         |
| Rec 5.2     | Companies should provide the information indicated in the Guide to reporting on Principle 5.                                                                                                                                                                                                                                                                                                                                                                                                         | ✓         |
| <b>Pr 6</b> | <b>Respect the rights of shareholders</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                            |           |
| Rec 6.1     | Companies should design a communications policy for promoting effective communication with shareholders and encouraging their participation at general meetings and disclose their policy or a summary of that policy.                                                                                                                                                                                                                                                                               | ✓         |
| Rec 6.2     | Companies should provide the information indicated in the Guide to reporting on Principle 6.                                                                                                                                                                                                                                                                                                                                                                                                         | ✓         |
| <b>Pr 7</b> | <b>Recognise and manage risk</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                     |           |
| Rec 7.1     | Companies should establish policies for the oversight and management of material business risks and disclose a summary of those policies.                                                                                                                                                                                                                                                                                                                                                            | ✓         |
| Rec 7.2     | The board should require management to design and implement the risk management and internal control system to manage the company's material business risks and report to it on whether those risks are being managed effectively. The board should disclose that management has reported to it as to the effectiveness of the company's management of its material business risks.                                                                                                                  | ✓         |
| Rec 7.3     | The board should disclose whether it has received assurance from the chief executive officer (or equivalent) and the chief financial officer (or equivalent) that the declaration provided in accordance with section 295A of the Corporations Act is founded on a sound system of risk management and internal control and that the system is operating effectively in all material respects in relation to financial reporting risks.                                                              | ✓         |
| Rec 7.4     | Companies should provide the information indicated in the Guide to reporting on Principle 7.                                                                                                                                                                                                                                                                                                                                                                                                         | ✓         |
| <b>Pr 8</b> | <b>Remunerate fairly and responsibly</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                             |           |
| Rec 8.1     | The board should establish a remuneration committee.                                                                                                                                                                                                                                                                                                                                                                                                                                                 | ✓         |
| Rec 8.2     | The remuneration committee should be structured so that it: <ul style="list-style-type: none"> <li>consists of a majority of independent directors;</li> <li>is chaired by an independent chair; and</li> <li>has at least three members.</li> </ul>                                                                                                                                                                                                                                                 | ✓         |
| Rec 8.3     | Companies should clearly distinguish the structure of non-executive directors' remuneration from that of executive directors and senior executives.                                                                                                                                                                                                                                                                                                                                                  | ✓         |
| Rec 8.4     | Companies should provide the information indicated in the Guide to reporting on Principle 8.                                                                                                                                                                                                                                                                                                                                                                                                         | ✓         |

## Glossary

**AGM** Annual General Meeting.  
**ASIC** Australian Securities and Investments Commission.  
**ASX** Australian Securities Exchange.  
**DPS** Dividends per share.  
**EBIT** Earnings before interest and tax.  
**EBITDA** Earnings before interest, tax, depreciation and amortisation.  
**EMEA** Europe, Middle East and Africa.  
**EPS** Earnings per share.  
**F10** Financial Year 2010: 1 July 2009 to 30 June 2010.  
**F11** Financial Year 2011: 1 July 2010 to 30 June 2011.  
**F12** Financial Year 2012: 1 July 2011 to 30 June 2012.

**FDA** United States Food and Drug Administration.  
**IFRS** International Financial Reporting Standards.  
**NPAT** Net profit after tax.  
**Previous GAAP** Previous Australian Generally Accepted Accounting Principles.  
**Processor/sound processor**  
 The externally worn part of the cochlear implant.  
**R&D** Research and development.  
**TGA** Therapeutic Goods Administration.  
**TSR** Total shareholder return.  
**TUV** Technical Überwachungs-Verein.

## Company Information

**Stock exchange listing**  
 Australian Securities Exchange  
 ASX code COH

**Solicitors**  
 Clayton Utz

**Share registrar**  
 Computershare Investor Services Pty Limited  
 Level 4, 60 Carrington Street  
 Sydney NSW 2000, Australia  
 Tel: 61 3 9415 4000

**Auditor**  
 KPMG

**Bankers**  
**Australia** Westpac Banking Corporation and HSBC Bank Australia Limited  
**Japan** The Bank of Tokyo-Mitsubishi UFJ, Limited  
**Sweden** Skandinaviska Enskilda Banken AB (publ)  
**United Kingdom** HSBC Bank plc  
**United States** Wells Fargo Bank West, NA

**Annual General Meeting**  
 The Annual General Meeting will be held at 10am on Tuesday 16 October 2012 at Australian Securities Exchange, Exchange Square Auditorium, 20 Bridge Street, Sydney. A Notice of Meeting and Proxy Form are enclosed with this Annual Report.

**Financial calendar**

|                           |              |
|---------------------------|--------------|
| <b>2012</b>               |              |
| Dividend record date      | 30 August    |
| Payment of final dividend | 20 September |
| Annual General Meeting    | 16 October   |

|                              |              |
|------------------------------|--------------|
| <b>2013</b>                  |              |
| Interim profit announcement  | 5 February   |
| Interim dividend record date | 22 February* |
| Payment of interim dividend  | 12 March*    |
| Final profit announcement    | 6 August*    |
| Annual General Meeting       | 15 October*  |

\* Indicative dates only.

Baha, Cochlear, Codacs, Hear now. And always, Hybrid, Nucleus, and the elliptical logo are either trademarks or registered trademarks of Cochlear Limited. iPhone is a registered trademark of Apple Inc. Android is a trademark of Google Inc.

**Design**  
 Cross Media Communications Pty Ltd

## Company ASX Announcement Record

**30 April 2012** *Cochlear to vigorously defend patent infringement complaint*

Cochlear Limited and its USA subsidiary Cochlear Americas have been named in a complaint filed by Adaptive Sonics LLC in Texas, USA. Cochlear believes that the allegations are without merit and intends to vigorously defend against the complaint.

**13 March 2012** *Half year report 2012*

Cochlear Limited provided an F12 half year report to shareholders listing half year revenues and sales.

**7 February 2012** *Record first half revenue*

Cochlear Limited announced revenue up 3% to \$387.5 million, with sales up 5% in constant currency for the six months ended 31 December 2011. There was a net loss of \$20.4 million after recall costs fully expensed. The interim dividend of \$1.20 per share was up 14%.

**7 February 2012** *Update on voluntary recall*

Cochlear Limited provided an update on the failure rate and mechanism related to the voluntary recall of the unimplanted Nucleus CI500 series implants.

**20 December 2011** *Update on voluntary recall*

Cochlear Limited provided an update on the root cause of failure related to the voluntary

recall of the unimplanted Nucleus CI500 series implants.

**18 October 2011** *Chairman's address*

Cochlear Limited Chairman, Mr Rick Holliday-Smith, addressed shareholders at the Annual General Meeting.

**26 September 2011** *Update on voluntary recall*

Cochlear Limited provided an update to shareholders on actions taken following the voluntary recall of the unimplanted Nucleus CI500 series implants.

**11 September 2011** *Voluntary recall of Nucleus CI500 cochlear implant range announced*

Cochlear Limited announced the voluntary recall of the unimplanted Nucleus CI500 cochlear implant range following a rise in implant failures from that range.

**9 August 2011** *Record financial results for year ended 30 June 2011*

Cochlear Limited announced revenue up 10% to \$809.6 million, with sales up 17% in constant currency. Net profit after tax was \$180.1 million, up 16%. The final dividend was \$1.20 per share (70% franked), up 14%.

## Non-IFRS financial measures

Given the significance of the product recall and FX movements the directors believe the presentation of non-IFRS financial measures is useful for the users of this document as they reflect the underlying financial performance of the business.

The non-IFRS financial measures included in this document have been calculated on the following basis:

- Excluding recall costs: IFRS measures adjusted for the costs of the product recall
- Constant currency: restatement of IFRS financial measures in comparative years using F12 FX rates
- Free cash flow: IFRS cash flow from operating and investing activities excluding interest and tax paid related to non-operating activities.

The above non-IFRS financial measures have not been subject to review or audit. However, KPMG have separately undertaken a set of procedures to agree the non-IFRS financial measures disclosed to the books and records of the consolidated entity.

Hear now. And always

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**Cochlear Medical Device (Beijing) Co Ltd** Unit 2208 Germdale Tower B, 91 Jianguo Road, Chaoyang District, Beijing 100022

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**Cochlear Limited** (Singapore Branch) 6 Sin Ming Road, #01-16 Sin Ming Plaza Tower 2, Singapore 575585 Tel: 65 6553 3814 Fax: 65 6451 4105

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**Cochlear Benelux NV** Schaliënhoedreef 20 1, B - 2800 Mechelen, Belgium Tel: 32 1579 5511 Fax: 32 1579 5500

**Cochlear Italia S.r.l.** Via Larga 33, 40138 Bologna, Italia Tel: 39 051 601 53 11 Fax: 39 051 39 20 62

**Cochlear France S.A.S.** Route de l'Orme aux Merisiers, Z.I. Les Algorithmes - Bât. Homère, 91190 Saint Aubin, France Tel: 33 811 111 993 Fax: 33 160 196 499

**Cochlear Nordic AB** Konstruktionsvägen 14, SE - 435 33 Mölnlycke, Sweden Tel: 46 31 335 14 61 Fax: 46 31 335 14 60

**Cochlear Tibbi Cihazlar ve Sağlık Hizmetleri Ltd. Sti.** Cubuklu Mah. Bogazici Cad., Bogazici Plaza No: 6/1, Kavacik

TR - 34805 Beykoz-Istanbul, Turkey Tel: 90 216 538 5900 Fax: 90 216 538 5919

**Cochlear Canada Inc** 2500-120 Adelaide Street West, Toronto, ON M5H 1T1 Canada Tel: 1 416 972 5082 Fax: 1 416 972 5083

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