

2016 COCHLEAR ANNUAL REPORT

Innovation for life



Hear now. And always



Cochlear®

Little sounds. Big sounds.

Life is full of sounds. Little sounds, big sounds, fun sounds, urgent sounds.

These sounds might be different for each of us, but whatever we do, and however we do it, we need to hear them.

In FY16, Cochlear continued to deliver products and services that help improve our customers' lives by making their hearing clearer, easier and more enjoyable.

We aim to give more people access to technologies that reflect their lifestyle. Our lifetime commitment means that when they eat out with friends, play sports or stream favourite movies from iPads, they get the hearing experience they want.

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Music is who I am. There is no reason
I have to give up anything at all.

Lindy Crocker
Recipient since 2013



Dr Lindy Crocker

- Musician, music teacher, Doctor of Philosophy
- Cochlear™ Nucleus® 6 recipient since 2013
- Enjoys integrated stereo sound with her Nucleus 6 sound processor and her GN ReSound hearing aid – ‘bimodal hearing’



Before, things were getting
harder and my world
was getting smaller.
Now, the future is bright.
And it sounds great!

Lindy Crocker



Chairman's Report



Rick Holliday-Smith Chairman

Cochlear reported a record net profit of \$189 million, an increase of 30% on the FY15 full year result. Earnings per share (EPS) increased by 29% to \$3.31 per share.

FY16 has been an important year for Cochlear involving renewal at the top level with incoming Chief Executive Officer & President, Chris Smith, transitioning into his new role, injecting a sharp focus on customer and market growth activities, while maintaining the Company's strong commitment to product development and innovation.

I have been pleased to see steady progress made throughout the year, with the suite of products launched over the past few years across all product categories laying the foundations for solid sales and earnings growth. Additional focus has been on more broadly reshaping the senior executive team with the addition of new and experienced talent.

It has also been a year where the balance sheet has been carefully reviewed and the new Chief Executive Officer & President has taken the opportunity to make some adjustments, as may be expected, in the first year of the new role. It has also been a year to continue the effort to focus on growth into the future and to make longer-term investments.

Dividends up 21%

Earnings growth, combined with strong free cash flow generation, has supported a 20% increase in the fully franked final dividend to \$1.20 per share. This takes dividends for the year to \$2.30 per share, fully franked, an increase of 21% on FY15. The dividend payout ratio of 70% of net profit is in line with the Board's target dividend payout ratio.

Australian company. Global presence

As a significant proportion of our activities are overseas, the Board meets each year in one of our global regions. This year we travelled to the United Kingdom (UK) and Europe and gained a stronger appreciation of the region generally, and the issues facing the UK and European markets, in particular.

Our business is performing well and we are confident that we have an appropriate strategy to grow over the coming years. We do however recognise that we are operating in an environment of global uncertainty as characterised by recent events including the UK's decision to withdraw from the European Union. While these events are not expected to have an immediate impact on our business, we remain alert to the potential for uncertainty to curtail economic growth and put pressure on health budgets.

The Board

During FY16 we involved an external consultant to independently review the Board with positive results in terms of the balance of backgrounds, experience and mix of tenure on the Board. We recognise the importance of undergoing a regular process of renewal

and from 2017 we will commence a process of Board renewal, ensuring we have a smooth transition of longer-serving Board members over the next few years.

Remuneration

Remuneration oversight of the Chief Executive Officer & President, the other key management personnel, and employees generally, is an important aspect of the Board's responsibilities. The role is carried out by the newly defined People & Culture Committee. The Remuneration Report sets out our approach to remuneration, and provides the FY16 details.

We need to ensure our remuneration practices are continually evolving to keep us competitive, ensure we can attract the best people, and effectively contribute to aligning performance and effort to our key business objectives. For FY17, we have introduced changes to our short-term incentives to strengthen alignment around global integration priorities under the banner of One Cochlear.

Building transparency and openness with shareholders

In FY16 we published a number of online shareholder reports aimed at improving transparency and making information easier to access. These include Cochlear's Corporate Governance Statement, Tax Contribution Report and Investor Handbook.

Cochlear's Corporate Governance Statement summarises the Company's corporate governance practices and incorporates the disclosures required by the ASX Corporate Governance Council's Corporate Governance Principles and Recommendations (3rd Edition). The Board is committed to achieving and demonstrating the highest standards of corporate governance. We continue to refine and improve the governance framework and practices in place to ensure they meet the interests of shareholders.

The Tax Contribution Report reports on Cochlear's taxes paid in Australia and globally and provides detail on our global tax strategy. Cochlear has a strong commitment to transparency and compliance from a regulatory and financial perspective and values the principles of being transparent with respect to its tax strategy and compliance in Australia and globally.

The Investor Handbook is an all-in-one reference for shareholders covering Cochlear's history, our global footprint, our product portfolio, the hearing loss market and how our products work, as well as providing summary financial information.

These publications are a great companion to the Annual Report and I encourage you to read them. They are all available at the Investor Centre of our website, www.cochlear.com.

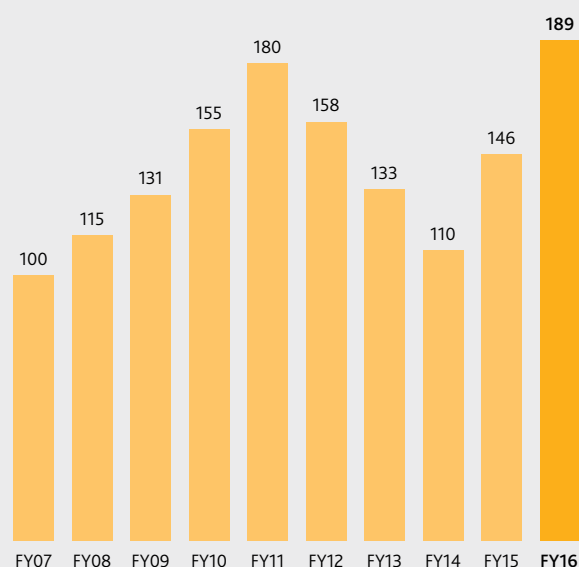
Our employees

We all recognise Cochlear has a diverse global workforce focused on our business and on transforming the lives of people with hearing loss. We employ around 3,000 people from over 75 nationalities, and we operate in 20 different countries. The knowledge, expertise and passion of our employees is key to our future and the focus on delivering excellence for our customers is an important part of our success and our market leadership position.

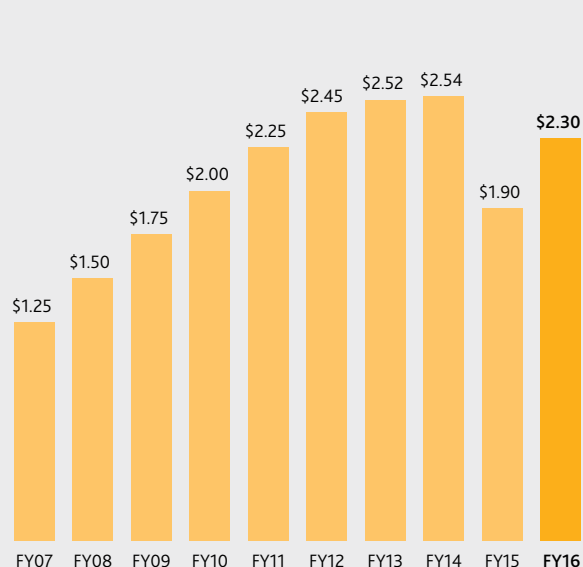
On behalf of the Board, I congratulate and thank all of Cochlear's employees for their outstanding efforts and contributions this year.

FY16 Performance Overview

Net profit adjusted^{1,2} ▲ **FY16 30%** on FY15



Dividends per share ▲ **FY16 21%** on FY15



10 year financial summary

	FY16	FY15	FY14	FY13	FY12	FY11	FY10	FY09	FY08	FY07
Cochlear implant system sales (units)	30,172	26,838	25,997	26,674	23,087	24,661	21,023	18,553	18,228	15,947
Total revenue (\$million)	1,131	926	805	753	779	810	735	695	602	559
R&D expenses (\$million)	143	128	128	125	119	109	95	97	80	66
EBITDA (\$million)	296	237	177 ²	202	239 ¹	270	244	206	193	171
EBIT (\$million)	263	206	150 ²	179	215 ¹	243	221	183	167	150
Net profit - adjusted (\$million)	189	146	110 ²	133	158 ¹	180	155	131	115	100
Net profit - reported (\$million)	189	146	94	133	57	180	155	131	115	100
Basic EPS (\$)	\$3.31	\$2.56	\$1.65	\$2.33	\$1.00	\$3.18	\$2.76	\$2.34	\$2.08	\$1.83
Dividends per share (\$)	\$2.30	\$1.90	\$2.54	\$2.52	\$2.45	\$2.25	\$2.00	\$1.75	\$1.50	\$1.25
Closing share price as at 30 June (\$)	\$121.25	\$80.15	\$61.70	\$61.71	\$65.84	\$72.00	\$74.32	\$57.70	\$43.65	\$61.00
Market capitalisation as at 30 June (\$million)	6,935	4,565	3,513	3,512	3,744	4,081	4,198	3,230	2,423	3,341
Number of permanent employees	2,934	2,632	2,536	2,531	2,390	2,319	2,006	1,888	1,789	1,655

1. Excludes product recall costs of \$139 million before tax and \$101 million after tax.

2. Excludes patent dispute provision of \$23 million before tax and \$16 million after tax.

The following non-International Financial Reporting Standards (IFRS) financial measures are included in this report:

- excluding patent dispute provisions;
- excluding product recall costs; and
- constant currency.

refer to page 90 for a discussion of these items.

Chief Executive Officer & President's Report



Chris Smith

Chris Smith
Chief Executive Officer & President

The positive momentum we saw in FY15 has continued throughout FY16 with strong growth delivered across all product categories and regions. The business achieved a major milestone with sales revenue increasing by 23% (12% in constant currency) to \$1.158 billion, exceeding \$1 billion for the first time.

The cochlear implant business delivered revenue growth of 21% (10% in constant currency) and unit growth of 12%. Our leading developed markets, including the United States (US), the United Kingdom (UK), Germany and Australia, each grew implant units by around 10%. Emerging markets performed well with highlights including China, both in the private pay and tender market, India and the Middle East.

We have strengthened our market-leading position with the success of a suite of product releases made over the past 18 months. In FY16 we introduced Cochlear's first off-the-ear sound processor Cochlear™ Kanso™; expanded the bone conduction portfolio with Baha® 5 Power and SuperPower sound processors; introduced the Nucleus® Profile™ Slim Modiolar electrode, the world's slimmest electrode and launched the next generation True Wireless™ Mini Microphone 2+.

Cochlear continues to demonstrate its commitment to being the technology leader in our industry with ongoing investment in research and development (R&D). Our aim is to improve hearing outcomes and expand the indications for implantable solutions so our recipients can have the quality of life they expect. In FY16, R&D spend increased by 12% to \$143 million, representing approximately 12% of sales revenue. As we move forward, we are injecting greater discipline into our R&D processes to ensure our investments are customer-driven and returns focused. We expect to deliver new products across all categories over the next 18 months as well as advance our long-term technology development pipeline.

The Services business, which includes sound processor upgrades and accessories, continues to perform well with sales revenue increasing 30% (20% in constant currency). Services now represents approximately 25% of sales revenue and has been established as a separate business unit. We expect its sales contribution to continue to trend upward over time as both the recipient base and service offering expand.

You can find a detailed review of the Product & Service Highlights and Regional Review on page 22.

Strong financial position

Cochlear has delivered a strong profit result with net profit of \$189 million, up 30%, the high end of the guidance range. Free cash flow remains strong and has supported the 21% increase in full year dividends.

We have benefited from the devaluation of the Australian dollar and have taken the opportunity to accelerate our investment in market growth initiatives, including direct-to-consumer marketing and expansion of the sales force, as well as increasing our investment in R&D. We believe these investments have contributed to market growth this year and will help underpin growth in the coming years.

At the same time, we have undertaken a balance sheet review in the context of new generation products launched over the past 18 months. The review has contributed to a \$16 million non-cash inventory write-off, pre tax, reflecting old and obsolete parts and products.

Our corporate strategy is centred on the customer

The hearing loss market offers an incredible business opportunity with over 360 million people worldwide experiencing disabling hearing loss, with nearly one in three people over the age of 65 affected by hearing loss.

With global market penetration for implantable hearing solutions less than 5%, there remains a significant, unmet and addressable clinical need that will continue to underpin the long-term sustainable growth of our business.

Hearing loss market



1. Who.int. WHO | Deafness and hearing loss [Internet]. 2015.

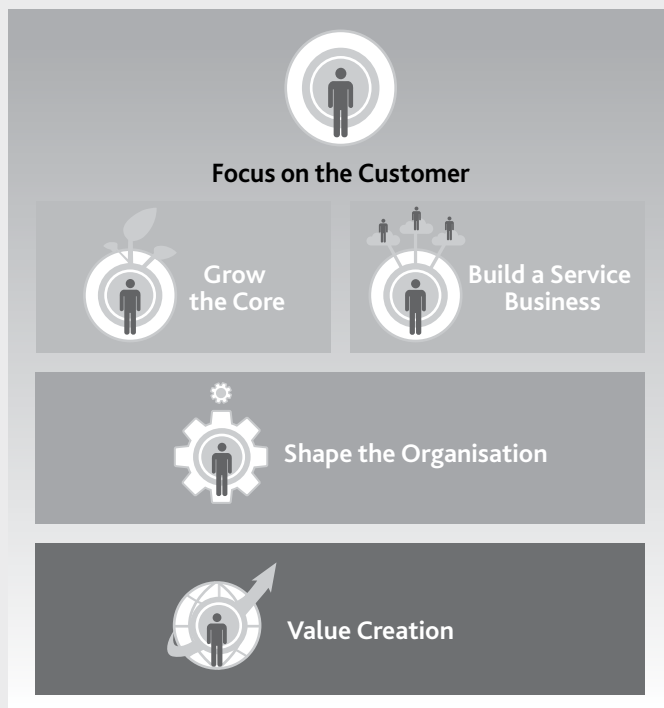
2. Who.int. WHO | 10 facts on deafness [Internet]. 2015.

3. Market penetration. This figure is a global estimate based on Cochlear sourced data.

* Disabling hearing loss refers to hearing loss greater than 40 decibels (dB) in the better hearing ear in adults and a hearing loss greater than 30 dB in the better hearing ear in children.

Our corporate strategy is centred on the customer

As Cochlear looks forward, priorities will be centred on the customer with activities aimed at expanding awareness and increasing patient access to the industry for implant candidates. And with a growing recipient base, now numbering over 450,000, the business is actively strengthening its servicing capability to provide products, programmes and services to support its lifetime relationship with recipients we well as drive revenue growth.



Grow the core

Implantable hearing devices will continue to be the driver of growth for the coming years. The focus will be to:

- strengthen the Company's technology leadership position. Over the next 18 months a series of new products are expected to be launched across all categories of the business focused on both share and market growth;
- stimulate market growth by increasing awareness of hearing loss, especially around severe to profound hearing loss, affecting nearly 40 million people world-wide. Over the last two years Cochlear has developed a direct-to-consumer marketing strategy in the US to target potential candidates, follow up leads and nurture candidates through the channel, which has contributed to higher market growth rates. Learnings from the US market are now being taken into other countries;

- improve access for candidates by expanding the cochlear implant clinic base as well as continuing to work with the referral channel to assist the Company's clinic partners to grow and become more efficient. The development of hybrid and acoustic implants, together with a broader range of electrodes, play an important role in broadening the indications for Cochlear's implantable hearing solutions; and
- business model innovation. Exploring new referral pathways and servicing models and where appropriate open Company-operated Cochlear clinics to manage the aftercare of recipients.

We have made solid progress in FY16. The highlights include:

- successfully introduced a range of new market-leading products including Kanso, Baha 5 Power and SuperPower, Nucleus Profile Slim Modiolar electrode and Mini Microphone 2+;
- appointed a Chief Medical Officer to expand clinical programs, enhance the regulatory path to market and strengthen the value proposition of Cochlear's products; and
- expanded the direct-to-consumer programs in the US and strengthened direct-to-consumer activities in other developed markets including in Australia, Germany and the UK.



Build a service business

With an ever growing base of recipients, now totalling over 450,000, Cochlear has both a lifetime responsibility and a significant business opportunity to service these recipients. Throughout the life of a recipient, Cochlear provides support with upgrades and services that improve their quality of life by improving hearing performance. The Company will:

- support the growing recipient base with upgrades, accessories and seamless recipient service and repair;
- increase connectivity and engagement with recipients with enhanced digital services; and
- introduce technology solutions for clinicians to help the Company's clinic partners grow and make aftercare for recipients more seamless.

The FY16 highlights include:

- established Services as a separate business unit and appointed a President;
- expanded the recipient recruitment program and clinical support tools with the roll out of Cochlear Family, MyCochlear.com and CochlearLink; and
- expanded the wireless product offering.



Shape the organisation

The organisation is being reshaped to better utilise and deploy resources to enhance capabilities, leverage best practice and improve the efficiency and effectiveness of operations and market initiatives. Cochlear will:

- expand its presence in customer facing activities across developed markets by expanding the field force and marketing activities to be closer to customers and clinic partners. The Company will also increase its presence in emerging markets like China;
- globally integrate enabling activities to fund market growth initiatives; and
- build organisational capabilities to support customer focused activities.

The FY16 highlights include:

- expanded the sales force across major markets with over 50 additional professional, clinical and customer-focused employees;
- expanded the sales office in Dubai to improve service in the Middle East and established an office in Vienna to service Central and Eastern Europe; and
- appointed a Chief Operating Officer to drive global integration of support functions and focus the organisation on operating as one global company to drive efficiencies and effectiveness.



Value creation

To deliver long-term sustainable growth, Cochlear will:

- develop alliances and partnerships, like the Smart Hearing Alliance with GN ReSound, that enable the Company to leverage its technology and leadership position to either expand the market or fast-track growth.

The FY16 highlights include:

- strengthened the Smart Hearing Alliance commercial relationship with GN ReSound; and
- established an innovation fund to focus on innovative technologies which potentially assist Cochlear's future business activities. \$14 million was invested in FY16.

2017 financial outlook

For FY17, net profit is expected to be within a range of \$210-225 million, an increase of around 10-20% on FY16. Cochlear expects positive momentum to continue, with investments made in product development and market growth initiatives expected to underpin growth for FY17.

Key considerations for FY17:

- expect continued strong uptake of the Nucleus 6 and Kanso sound processors over the next few years with the current penetration rate for the Nucleus 6 at around 22% of potential recipients;
- Chinese Central Government tender units expected to be at similar levels to FY16 with delivery of units biased to the first half;
- in Europe, Cochlear does not expect any immediate impact on the business from the UK's decision to withdraw from the European Union. However, the Company remains alert to the potential for uncertainty to curtail economic growth and put pressure on health budgets;
- expect FY17 R&D expenditure to be broadly in line with that for FY16, representing a lower percentage of sales revenue;
- forecasting a weighted average AUD/USD FX rate of 75 cents for FY17 versus 73 cents in FY16; and
- the balance sheet position and free cash flow generation remain strong. The Company will continue to target a dividend payout ratio of around 70% of net profit.

Environment, Social and Governance (ESG)



Supporting environment awareness activities

Our approach to ESG reflects the Company's commitment to excellence. The importance we place on ESG issues can be seen in the work we do to deliver quality, innovative products and services.

Cochlear is involved in a range of ESG related activities and initiatives, some of which are highlighted in this report.

High performance and strict legal compliance on environmental, privacy and safety issues are also integral to our culture. For more information on Cochlear's Governance reporting, see our Corporate Governance Statement 2016, which is available on Cochlear's website, www.cochlear.com.

Our products and performance reflect the quality of our people. We seek the best people and support them to be successful in their work. We are proud of our environmental and governance record as well as our social contribution.

Cochlear follows a global Code of Business Conduct, which helps us best serve our recipients and give them the best hearing possible.

Environmental awareness

Cochlear is committed to improving the lives of its recipients, driving innovation within the medical device industry, and in doing so, promoting best practice business principles.

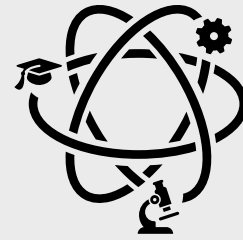
Property footprint

Cochlear seeks to ensure that global offices reflect Cochlear's commitment to creating and maintaining consistent and high quality work environments. We have prepared guidelines to help with establishing work environments that are efficient and effective in the use of space and resources, utilising environmentally sustainable materials and conducive to productivity.

Cochlear Limited global headquarters

Cochlear's global headquarters on the Macquarie University campus, Sydney, which also houses our Asia Pacific regional headquarters, was awarded a 4 Star Green Star rating by the Green Building Council of Australia, confirming good practice in environmentally sustainable design/construction of the building.

The headquarters building achieved a rating equivalent to a 5 star NABERS rating¹ (carbon emissions associated with electricity and gas consumption are 270% better than those for an "average performance" building). This high rating was achieved through a high efficiency façade design, energy efficient lighting and an innovative air conditioning system.



Engaging with universities and research groups

Water efficient fittings and fixtures have been used throughout the building. The building reuses rainwater that is collected from the roof and is stored in underground reuse tanks. The tanks have a capacity of 350 cubic metres. The water is filtered and then used to supply all the toilets and the cooling towers within the building and used to irrigate the landscape outside.

The waste recycling systems in place at the Sydney headquarters include:

- commingle recycle waste collection in all break-out and kitchen areas, collecting approximately 20 tonnes a year;
- paper and recyclable collection at workstations and utility areas;
- 1 x 10 tonne cardboard compactor, replaced approximately every three months;
- battery recycle collection, collecting approximately 225 kilograms of waste a year;
- used machine oil recycling of approximately 2,000 litres per year;
- e-waste recycle collection, collecting approximately 600 kilograms of waste a year;
- fluorescent tube recycling, collecting approximately 400 kilograms of waste a year;
- 240 litre capacity security paper destruction bins, collecting approximately 180 bins a year; and
- pallet recycling of approximately 300 wooden pallets per year.

We maximise office recycling, for instance with batteries, toner cartridges and used IT equipment, by providing employees with instructions as well as clear stations for materials to be collected.

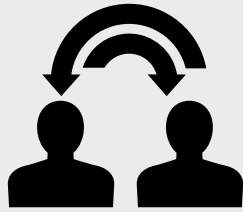
We encourage cycling to work and a reduction in car use, by providing 160 bicycle parking spaces as well as change rooms and bike storage facilities. Carpooling is encouraged with 11 car spaces allocated for users.

One of Cochlear's key procurement principles is the requirement to consider the economic, social and environmental impact when acquiring goods or services from selected suppliers.

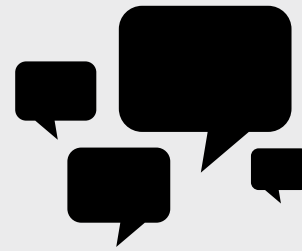
Consideration where appropriate is given to energy usage, emissions, water usage, resource use, waste generation, recyclability, toxicity, biodiversity, land use, social responsibility, economic viability, innovation and health and safety.

1. NABERS (National Australian Built Environment Rating System) is a national rating scheme managed by the NSW Government in Australia.

Environment, Social and Governance (ESG)



Encouraging participation in national debate



Increasing global awareness of hearing loss

Cochlear Bone Anchored Solutions (CBAS) headquarters

The CBAS headquarters in Mölnlycke, Sweden, makes extensive efforts to reduce electricity use and waste.

The business works with Sweden's leading recycling and environmental company, Ragn-Sells, to ensure best environmental practice. This involves a commitment to continuously improve waste separation and ensure that whenever possible waste products are reused, recycled or used for energy recovery before disposal.

Waste sorting includes for:

- combustibles;
- office and confidential paper;
- corrugated paper;
- metallic packaging;
- shrink and stretch wrap;
- glass;
- sharps;
- electronics;
- small batteries;
- light bulbs;
- wood;
- mixed waste;
- dangerous goods (chemicals); and
- toners.

We also place focus on the supply chain so that all transport is conducted in an environmentally safe and efficient manner.

The CBAS building has been awarded a Green Building Silver Certificate by the Sweden Green Building Council.

Designed for Swedish conditions, the Green Building Certificate system certifies buildings in terms of energy efficiency, indoor climate and materials. The system has been developed by researchers in collaboration with companies in the construction and real estate industries. The system gives the awards of Gold, Silver or Bronze Certificates and are used for both residential and commercial premises.

A Green Building Silver level fulfils mainly demands for highly efficient use of energy, healthy materials, good indoor environment, good ventilation and high moisture resistance.

Cochlear Technology Centre

The Cochlear Technology Centre in Mechelen, Belgium, which is Cochlear's largest R&D facility outside Australia, makes similar efforts to reduce the operation's impact on the environment. Showers and lockers have been installed to encourage cycling to work and sport at lunch time. Company cars are costed proportionally to carbon gas emissions, to encourage employees to choose more environmentally-friendly cars. Sun protection film on all windows reduces the need for cooling.

Special 'waste lanes' have been created to more efficiently separate and collect recyclable materials. Batteries, electrical devices and wooden pallets are also collected separately.

Cochlear Americas headquarters

In our regional headquarters in Denver, US, an extensive ongoing program is run to boost environmental sustainability and ensure compliance with the requirements of local authorities. Some of these activities include:

- installation of sink fixture aerators in the rest rooms to reduce water consumption;
- single source recycling in all kitchens, break rooms and printer stations to reduce waste going to landfill;
- use of a cardboard compactor for all used boxes; recycling of all fluorescent bulbs (per United States Environmental Protection Agency mandate); and
- recycling of all used or out-of-date batteries and e-waste.

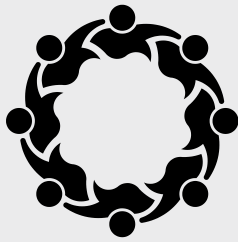
The office has locker rooms with shower facilities to allow individuals to cycle to work or exercise during off hours.

Cochlear Europe, Middle East and Africa (EMEA) headquarters

Cochlear has undertaken two key initiatives to promote environmental sustainability in our EMEA headquarters in Basel, Switzerland.

These comprise:

- a new agreement with an energy provider to use power from renewable energy sources; and
- office-wide education programs to reduce workspace and IT energy usage.



Supporting employee participation in community fundraising and activities



Educating visitors to headquarters with facility tours

Manufacturing

The majority of Cochlear's manufacturing is located at the global and CBAS headquarters sites. Cochlear actively manages all inputs and outputs to promote environmental best practice.

Cochlear holds environmental licences governing generation and control of waste and pollution in Australia. Cochlear retains or recycles nearly all of its waste product material from manufacturing in Australia.

A lean philosophy in Cochlear's manufacturing process, which is a systematic method for the elimination of waste. This enables us to reduce overproduction, reprocessing and defects, and increase recycling and paperless operation documentation. Redesigned packaging and flexible printing have also reduced packaging waste.

Social support

Supporting the tertiary education sector

Cochlear is a knowledge based organisation and strongly supports and engages with the tertiary education sector.

The Australian Hearing Hub is adjacent to Cochlear's global headquarters at Macquarie University. The Hub brings together over 2,000 people, across a range of disciplines, dedicated to promoting hearing health.

The Cochlear Clinical Skills Institute, a world-class surgical training centre in the Australian Hearing Hub, was recently opened and Cochlear's Australian and New Zealand sales office has moved there to be close to key customers.

There is a range of activities where Cochlear engages with Macquarie University, including placement opportunities for students, guest lecturing and public advocacy. There are also a number of research projects underway involving both organisations, into areas such as engineering, computing, audiology, linguistics and cognitive science.

Cochlear has research agreements and arrangements with over 100 external research partners around the world. Cochlear's support is focused on increasing the understanding and treatment of hearing loss.

Cochlear is a core member of The HEARING Cooperative Research Centre based in Australia, which combines academic, business and government interests to further understanding and development of technologies for diagnosis and remediation of hearing loss. Since 2007, 38 students have engaged in postgraduate doctoral studies in hearing related topics under this scheme.

Supporting the community

In 2007, the Cochlear Foundation was established to promote community leadership and the awareness of, and research into, treatments for hearing loss. The foundation has provided support for a range of projects including STELR (Science and Technology Education Leveraging Relevance), an initiative to advance Science, Technology, Engineering and Mathematics (STEM) education.

The Cochlear Foundation also supported other Australian educational awareness activities in FY16 as well as charity events and clinical research associated with the treatment of hearing loss.

Cochlear encourages its employees to participate in volunteering and community fundraising and corporate sporting activities and directly supports its employees in a number of activities. Employees who are engaged in eligible community service activities are granted time off.

In Europe, Cochlear supported community activities in several countries in FY16 through team involvement and financial help.

In the United States, Cochlear continues its support of several non-profit hearing loss organisations including the Hearing Loss Association of America, AG Bell, Ear Community, Songs for Sound and the American Cochlear Implant Alliance. During FY16, scholarships were awarded to eight gifted students in the US who have overcome hearing loss and achieved academic and personal success. Cochlear has awarded more than US\$568,000 in scholarships to 80 college students in the US since 2002.

Supporting employees

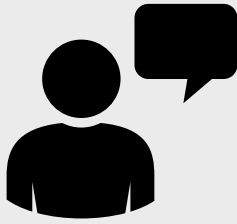
Cochlear's global team operates in safe and healthy work environments. Numerous workplace health and safety activities are undertaken and support is provided for healthy living initiatives as well as access to a range of health services.

More information can be found in the People and Culture section of the Annual Report.

Industry and advocacy

Cochlear has many professional staff involved in helping relevant research and community programs in their regions, partnering with academic, industry and health professionals to assist Cochlear recipients gain access to services and support and also advocates for resources for the institutions that support them. This is particularly important in developing countries.

Environment, Social and Governance (ESG)



Introducing Cochlear Global Hearing Ambassador

Many Cochlear employees are engaged in advocacy to improve hearing health policies around the world.

Cochlear proactively supports the World Health Organisation's global effort to highlight the need for prevention and treatment of hearing loss.

Cochlear encourages its executives to participate in forums and bodies that advance Australia's competitiveness and the promotion of innovation and technology.

Hearing loss awareness

Hearing loss is a global public health issue and Cochlear is engaged in raising awareness of it and the relevant treatments available to address it.

In Australia and New Zealand, Cochlear sponsored the Power of Speech public speaking competition for deaf children to challenge the common perceptions of what a deaf child can achieve. Cochlear has also set up and works closely with the Cochlear Awareness Network of volunteers who connect candidates in the community and offer support.

On 25 February, Cochlear launched a global social media campaign for International Cochlear Implant Day to celebrate the successes of people with Cochlear implants using the hashtag #CelebrateCochlear.

International Ear Care Day is an annual advocacy event held on 3 March. In 2016, it was elevated in status by the World Health Organisation to World Hearing Day and aims to raise awareness, and promote ear and hearing care across the world. The theme for World Hearing Day 2016 was 'Childhood hearing loss: act now, here is how!'. Macquarie University, with Cochlear's support, issued a media release calling for more action on hearing loss by governments, communities and individuals.

On World Hearing Day, comprehensive education and awareness activities took place in Australia, the UK, Benelux, Poland, Ukraine, Russia and Lebanon.

In May, the Australian Deafness Forum and partners launched a national campaign, Break the Sound Barrier, in Australia to call for hearing loss to be made the 10th national health priority.



Offering tiered products in developing markets

Every year, Cochlear supports Hearing Awareness Week in August to raise awareness of hearing loss and treatments for hearing loss, such as Cochlear implants, especially among adults.

Cochlear's Global Hearing Ambassador, Brett Lee, launched the Sounds of Cricket campaign in the UK, the Middle East, India, Sri Lanka and Australia. The campaign draws attention to hearing loss through the iconic sounds of the game watched by a quarter of the world's population. The campaign has generated extensive media coverage and social media engagement, especially in India. Brett has used his personal experience with his son's hearing loss to drive public awareness of the issue.

Cochlear makes an effort to educate visitors to its headquarters by giving tours of the facility and providing information about the significant medical, social and economic impacts of hearing loss. Plans are underway for a new hi-tech, interactive tour to enhance this experience.

Cochlear Americas initiated a Million Ear Challenge campaign for Better Speech and Hearing Month (May) that urged people to share the facts about hearing loss with one million people via social media. The campaign teamed up with the Hearing Loss Association of America in over 20 awareness events (Walk4Hearing). The team also held over 90 Hearing Health Seminars to educate people on hearing loss and Cochlear solutions.

Access to healthcare

Cochlear sells its products in over 100 countries. Cochlear provides, particularly in emerging markets, support to professionals in the healthcare area. We facilitate partnering of surgeons and supporting education of local professionals. Part of enabling access to our products in developing markets is our ability to provide tiered products to suit the needs and financial ability of customers.

Governance

Cochlear's key corporate governance principles and practices are outlined in the Corporate Governance Statement 2016, which is available on Cochlear's website, www.cochlear.com.

Innovation for Life

Cochlear continues to make investment in innovation a priority so as to deliver products and services that best meet our customers' needs. Cochlear has invested more than \$600 million in global R&D activities over the past five years. In FY16, Cochlear's total R&D investment was \$143 million, which was around 12% of sales revenue.

More than 350 specialists from a range of technical disciplines are employed in the Company's Design and Development department. These teams are based in Australia, Belgium, Sweden and the United States. Cochlear also works with over 100 external research partners based in 20 countries.

Cochlear continues to develop solutions that drive improved hearing performance outcomes, improved lifestyle solutions and expanded indications for candidates and recipients of the Company's products. Research covers scientific research, new technology development and new product development. This includes work on Cochlear's sound processing algorithms, electrode technology, totally invisible hearing implants, wireless connectivity, biology research and the continued expansion of Cochlear's portfolio of implantable hearing devices.

The Company also continues to expand its offering of clinical care tools that support professionals with a growing set of options to manage their customers, including cloud based connection technologies.

Product highlights during FY16 included:

- CE approval and market introduction of Kanso;
- CE, Canada Health and FDA approval of the Cochlear Nucleus Profile Implant with Slim Modiolar electrode (CI532), including regulatory approval and roll-out in the US;
- CE and FDA regulatory approval of the Cochlear True Wireless Mini Microphone 2 and Mini Microphone 2+;
- CE and FDA regulatory approval of the Cochlear Nucleus Profile Auditory Brainstem Implant (ABI541) and market introduction;
- market introduction of Cochlear Custom Sound 4.3 and Nucleus Fitting Software 1.4;
- market introduction of Cochlear Baha 5 Power and SuperPower sound processors, to complete the Baha 5 portfolio;
- market roll-out of the next generation of Cochlear Baha 5 smart App for iPhone and for Android;
- market roll-out of the next generation Cochlear Baha Fitting Software 5.2; and
- continued market development and roll-out of Cochlear's acoustic implants in Europe and Latin America.

Manufacturing and supply chain operations

Cochlear has a global supply chain with sales into more than 100 countries. Components are sourced across Europe, Asia and the Americas. Manufacturing operations are primarily located in Australia and Sweden, with smaller sites in Belgium and the US. Suppliers and the manufacturing sites are aligned to enable the Company to deliver products of the highest quality and reliability.

The structure and execution of the supply chain play an important part in our customers' experience as well as for the introduction of new products and technologies. Over 1,000 people are currently employed in Cochlear's manufacturing facilities around the world.

The Company's manufacturing strategy is to make sure that capacity production methods deliver the highest quality products to meet demand whilst at the same time improving the operational efficiency. To achieve this, Cochlear adopts continuous improvement programs, which incorporate lean manufacturing principles and ongoing investment in new manufacturing technologies. These programs are designed to deliver the capacity, flexibility and productivity to satisfy our customer requirements.

Non-military use

Other than where our products are used by military personnel, Cochlear produces or contributes to no products or services designed or used for military purposes.

Quality management system

Cochlear has implemented a quality management system to ensure the quality of its products and services. This system is regularly assessed by external regulators. Certificates include (but are not limited to): ISO 13485, ISO 9001, Medical Device Directive and Active Implantable Medical Device Directive.

Device approvals

Medical devices must be approved by relevant regulatory authorities. At present, Cochlear (or an affiliate or distributor/representative) has the necessary licences and approvals to enable the marketing of each product in the jurisdictions in which the product is marketed. Ongoing approvals are regularly being sought for new products in a variety of jurisdictions.

Intellectual property

The creation and protection of our intellectual property remain a key strategic imperative for the business. Cochlear currently holds over 1,100 patents and patent applications globally, and filed many new patent applications in FY16.

People and Culture

Cochlear delivers industry leading products and services through a highly skilled, passionate workforce of approximately 3,000 people in over 20 countries.

Cochlear people represent a diverse range of disciplines, nationalities and working styles all dedicated to our mission. Our people strategies focus on engaging everyone in delivering the mission, aligning to our business priorities and building capabilities to deliver future growth.

Our People

Cochlear strives to attract and retain passionate and highly skilled professionals. We achieve this through interesting and challenging work, the opportunity for development within a growing business but most importantly through our passion to achieve a common purpose – our mission. We have a high level of engagement built on our shared goals to improve the experience we provide to our customers.

In FY16, we continued to be an Employer of Choice, attracting over 18,000 applications from around the world to fill just over 500 permanent and fixed-term positions, a record for the company. The Company maintains high staff retention levels with global annualised turnover under 10%, which is low by industry standards.

Over the year, Cochlear continued to focus on building the capabilities of our workforce to meet business needs by promoting from within and providing employees with opportunities to build their careers. In FY16, 29% of positions were filled internally. The year saw an increase in the number of employees moving internationally to broaden their experience and facilitate learning and sharing.

At the executive level, we had nine appointments over the year:

- Chief Executive Officer & President, Chris Smith, formerly the President, Americas Region;
- Tony Manna, President, Americas Region, formerly General Manager, CBAS;
- Rom Mendel, General Manager, Cochlear Acoustics, formerly General Manager CBAS;
- David Hackshall, Chief Information Officer, joining Cochlear from Wesfarmers Insurance;
- Dig Howitt, Chief Operating Officer, moving from President, Asia Pacific Region. This position was created to support the integration and alignment of Cochlear's global operations and to ensure efficiencies and effectiveness are maximised as the Company grows globally;
- Stu Sayers, inaugural President, Services. The Services business provides aftercare support, product and direction for cochlear implant recipients. It generates revenue from the sale of sound processor upgrades and accessories as well as focusing on the development of software solutions that will serve our customer over a lifetime;
- Dr Rich Toselli, inaugural Chief Medical Officer. Rich will lead the Global Clinical and Regulatory teams, bringing greater global coordination and integration of these activities as well as leading Cochlear's Health Economics and Outcome Research activities;

- Amanda Lampe, Senior Vice President, Corporate Affairs, Strategic Alignment and Public Health, moves from SVP Global Marketing. The new role will build public health policy advocacy and hearing loss awareness initiatives, lead global alignment of communications and coordinate and deliver corporate strategy;
- Dean Phizacklea, Senior Vice President, Global Marketing, bringing to Cochlear many years of marketing experience with both the medical device and pharmaceutical industries across the world; and
- Katharine McLennan, Senior Vice President, People & Culture, responsible for building out Cochlear's strategic capability in talent management, acquisition, development, remuneration, performance, engagement and succession planning.

Cochlear has continued its commitment to developing a strong talent pipeline for future growth, employing the largest cohort of engineering summer students since the program began in 2008.

In February 2016, we welcomed a record number of graduates who were selected from the students who completed the summer student intern program in the summer of 2014/2015.

In FY16, we launched our first ever Graduate Lawyer program. Throughout the year, Cochlear also hired new employees into new and specialised skill areas to support key global projects, transforming our customer experience and communications capabilities.

Cochlear employs a highly flexible workforce in our manufacturing department by providing ongoing opportunities for job enrichment through the Manufacturing People Program. Our Learn about Cochlear program connects the manufacturing workforce with our recipients to ensure we are regularly focusing on our customers.

We celebrate a highly diverse workforce and consult and engage regularly through our Employee Communications Committee, providing a forum for collaboration between the manufacturing and leadership groups.

Development

Cochlear continues to invest in employee development programs to help individuals and enhance organisational capabilities. During the year, we launched a new approach to goal setting and performance called My Performance Pathway.

My Performance Pathway is designed to increase employee engagement by helping employees to create strategically aligned goals. The program includes a focus on building the skills of people managers to help their teams set goals and coach them in achieving their goals on a regular basis.

Performance in Cochlear means not only what employees achieve in outcomes but how they achieve it with our new HEAR behaviours, which we expect all employees to exhibit:

- Hear the customer;
- Embrace change and innovate;
- Aspire to win; and
- Remove boundaries.

Cochlear accelerated its development of leadership capability amongst its global executive cohort with a total of 78 Cochlear leaders completing programs in Leading Innovative Change, Leading Strategic Growth and Leading Operational Excellence. This development was aligned to key business projects, to facilitate rapid transfer of learning back to the workplace and to ensure leaders are supported and equipped to move our business forward.

Improvements to our learning management system have delivered an even stronger learner experience for employees, providing employees with access to an expanding range of learning programs through different media. Manufacturing Academy was further rolled out to support the delivery of training and skill-building processes in our manufacturing environment in Brisbane.

Diversity

As a global business, Cochlear strongly encourages all forms of diversity to support our leadership and innovation strategies. In our Sydney offices, employees come from 75 different countries and approximately 80% of our workforce was born outside Australia.

The Company's global workforce is 51% female and women make up 34% of our senior manager population. Of the new permanent employees recruited globally in FY16, 57% were women. This outcome was achieved even though 37% of all job applicants were women.

During FY16, Cochlear maintained programs to promote diversity in its workforce, including support for the Women in Leadership initiative, Leadership Presence programs aimed at developing the pipeline of female leaders at Cochlear and Talent planning also focused on engendering a more diverse talent pipeline.

We consider gender and STEM talent needs in all talent process design, and we measure and monitor outcomes to continuously improve our employee value proposition and minimise any potential sources of bias in areas like selection, promotion and performance assessment and reward.

Health and Safety

Cochlear always seek to provide innovative Health and Safety solutions to enhance the working and personal lives of all our people.

Cochlear views Health and Safety as an integrated element of our overall operations and seeks to involve all levels of the organisation in the solutions and continual improvement of all aspects of the execution of Health and Safety.

During FY16, the Australian operations expanded on last year's introduction of the Enterprise Risk Management solution, refining the elements of the Risk Management and Inspection and Audit Modules. These two modules will increase the capability of our people to participate in the ongoing continual improvement of the management of risk at Cochlear.

The Health and Safety team and personnel from Design, Engineering, People and Culture and Production collaborated substantially across the year to look closely at the process of design and manufacture to improve Health and Safety outcomes for production personnel and drive efficient processes. This will contribute to the continued drive for improvement of the production process to be safer and more efficient.

The Health and Safety team provided support and expertise to coach and collaborate with all personnel, driving improvement in risk management, hazardous substances and emergency management across the organisation. FY16 saw the focus on safe, simple and collaborative process, building a responsive and flexible framework for personnel to operate within.

Workers compensation and health insurance premiums have reduced substantially across the organisation and we are tracking favourably against our comparative industry; the continued improvements in the manufacturing process should see this favourable trend continue.

Wellness continues to be a focus across the organisation and the provision of preventive programs to enhance wellness was offered to all personnel, with a focus on physical, social, financial and occupational wellness. Lifestyle programs, vaccinations and support for external events, sports and challenges were provided during FY16.

The provision of an Employee Assistance Program as a resource to all personnel and eligible family members is a continuing priority. All aspects of wellness and wellbeing are a continuing and very high priority and will play an increasing factor in how Cochlear will differentiate itself in talent attraction and retention.

Our Culture

Most important to all that we do is our focus on a culture of One Cochlear, which is about:

- integrating our operations, strategy and behaviour across our 25 countries;
- standardising our processes;
- collaborating across the world to generate new ideas and better ways of working; and
- sharing resources to drive innovation, effectiveness and efficiency.

We are building out our talent mobility as we begin to create "global citizens" whose functions, presence, influence and travel cover the world. We are increasingly globalising all of our functions as our global footprint continues to expand.

In FY16, we began the process of globalising our approach to IT, quality, talent management, repair, manufacturing and inventory management, and we will extend this process to all of our functions in the coming year.

Having created the approach to My Performance Pathway, we have further reinforced One Cochlear by setting 12 global goals so that all 3,000 employees can align their individual goals commonly, understand how they fit across the world of Cochlear, and identify their counterparts and collaborators across the world.

Now more than ever before, we will insist all of our people know our end customers' needs, desires and motivations as we expand the education, experience and exposure we give our people to our customers, our audiologists, our reimbursement parties and our surgeons all over the world. Hearing the customer is at the core of everything we do – and we are now instilling the importance of candidates and customers that we serve for their lifetime, which is at the heart of our mission.

Board of Directors

1. Rick Holliday-Smith

Age 66. BA (Hons), FAICD, CA

Appointed 1 March 2005. Eleven years' service.

Director of Servcorp Limited since 1999. Director of ASX Limited since 2006 and Chairman since March 2012. Former Chairman of Snowy Hydro Limited (not publicly listed) (2006–2012) and 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 Board of Directors and Nomination Committee. Member of the Audit and People & Culture Committees.

2. Chris Smith

Chief Executive Officer & President

Age 53. BSc

Appointed 1 September 2015. Nine months' service.

Joined Cochlear in 2004. Has more than 20 years' experience in the healthcare and medical device industry in the United States including assisting Warburg Pincus in identifying market opportunities for investment. Prior to this, was Group President for Gyrus Group (ENT and Surgical Divisions). Previous Cochlear roles include President, Americas Region and Senior Vice President, Cochlear Bone Anchored Solutions and Global Support Operations.

Member of the Medical Science and Technology & Innovation Committees.

3. Yasmin Allen

Age 52. BCom, FAICD

Appointed 2 August 2010. Six years' service.

Director of Santos Limited and member of the Santos Environment, Safety and Sustainability Committee and Audit Committee. Director of ASX Limited and member of ASX Audit Committee and ASX Clearing and Settlement Board. Director of National Portrait Gallery since 2013. Member of the George Institute for Global Health Board.

Former Director of Insurance Australia Group Limited (IAG). Former National director of the Australian Institute of Company Directors. Former member of The Salvation Army Advisory Board. Former Chair of Macquarie Specialised Asset Management. 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 People & Culture, Nomination and Technology & Innovation Committees.

4. Prof Edward Byrne, AC

Age 64. DSc, MD, MBA, FRCP, FRACP, FTSE

Appointed 1 July 2002. Fourteen years' service.

Chairman of King's Health Partners. President and Principal of King's College London since 1 September 2014. Former Deputy Chairman of Group of Eight Vice Chancellors, Australia, and Chairman of Global Foundation. Former director of Bupa Group Board, London and Bupa Australia Pty Limited. Former Vice Chancellor of Monash University (June 2009 – August 2014). 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).

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

5. Andrew Denver

Age 67. BSc (Hons), MBA, FAICD

Appointed 1 February 2007. Nine years' service.

Chairman of Universal Biosensor Pty Limited since 2005 (director since 2002) and SpeedX Pty Limited since 2009. Director of Vaxxas Pty Limited since 2012. Former director of Principals Cornerstone Management Pty Limited. Former Managing Director of Memtec Limited and President Asia for Pall Corporation.

Chairman of the Technology & Innovation Committee. Member of the Audit, Medical Science and Nomination Committees.

6. Donal P O'Dwyer

Age 63. BE Civil, MBA

Appointed 1 August 2005. Eleven years' service.

Chairman of Atcor Medical since 2004 and a director of Mesoblast Limited since 2004 and Fisher & Paykel Healthcare Limited since 2012. Non-executive Director of NIB Holdings Ltd since 2016. Former director of Sunshine Heart Inc (2004–2013). Former Worldwide President of Cordis Cardiology (Johnson & Johnson medical device business unit) between 2000 and 2004.

Member of the Audit, Medical Science, Nomination and Technology & Innovation Committees.

7. Glen Boreham, AM

Age 51. BEc, FAICD

Appointed 1 January 2015. Eighteen months' service.

Director of Southern Cross Austereo since 2014 and Link Group since 2015. Chairman of Advance since 2012 and the Industry Advisory Board for the University of Technology, Sydney, since 2010. Former Director of Data#3 (2011–2015). Former Chairman of Screen Australia (2008–2014). Former Managing Director of IBM Australia and New Zealand (2006–2010).

Chairman of the People & Culture Committee. Member of the Audit, Nomination and Technology & Innovation Committees.

8. Alison Deans

Age 48. BA, MBA, GAICD

Appointed 1 January 2015. Eighteen months' service.

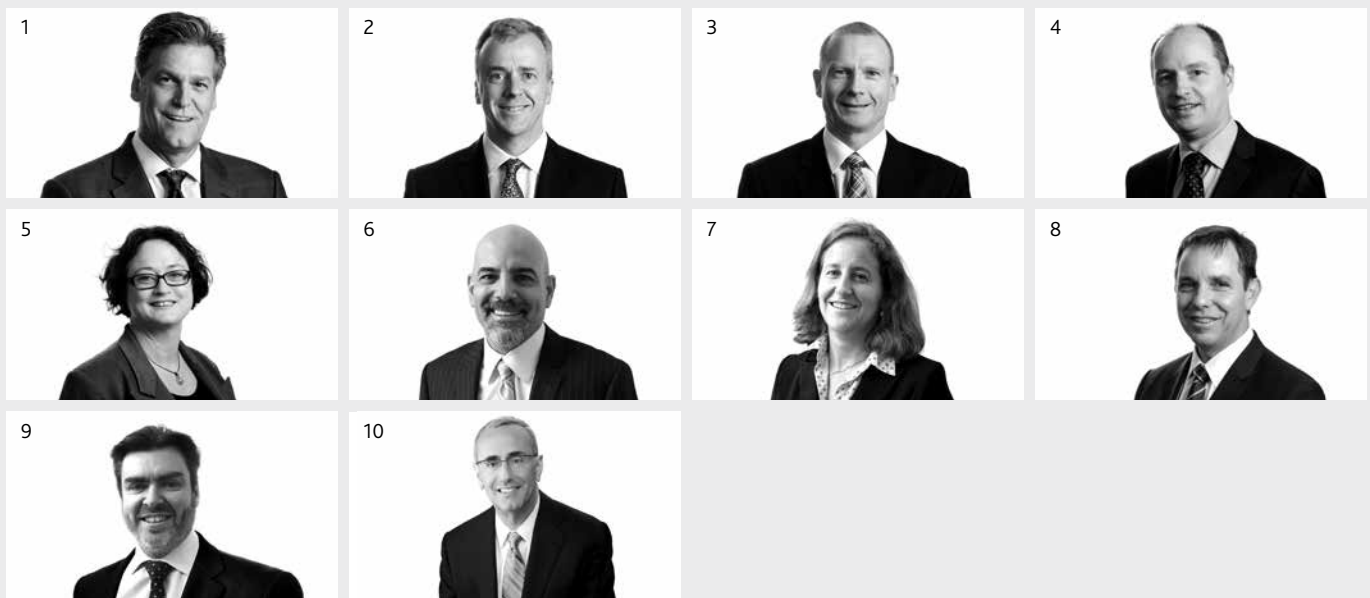
Director of Westpac Banking Corporation since 2014, Insurance Australia Group Limited since 2013 and kikki.K Holdings Pty Limited. Former Chief Executive Officer of the technology-based investment company Netus Pty Limited (2006–2013), Hoyts Cinemas (2003–2004), eCorp Limited (2000–2003) and eBay Australia and New Zealand (1999–2000).

Member of the Audit, People & Culture, Nomination and Technology & Innovation Committees.

Board of Directors



Senior Executive Team



1. Chris Smith

*Chief Executive Officer
& President*

See "Board of Directors" on page 16.

2. Richard Brook

*President, Europe, Middle East
and Africa 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 (EMEA) and Latin America. This includes sales in over 60 countries. Operations in EMEA and Latin America include sales,

marketing, distribution, service, finance, clinical, regulatory and administration across these complex and diverse regions.

Before joining Cochlear in 2003, Richard held senior roles in Guidant Corporation and Alaris Medical Systems. He has over 20 years' experience in the medical device industry.

3. Dig Howitt

Chief Operating Officer

BE (Hons), MBA

Dig was President, Asia Pacific Region in FY16 and was appointed Chief Operating Officer (COO) in July 2016. The COO will support the

integration and alignment of Cochlear's global activities to ensure efficiency and effectiveness are maximised as the Company grows globally. Functions included in the COO remit include global marketing, global IT, global quality, global supply chain, Bone Conduction and Acoustics. Dig will also retain responsibility for the China business.

Dig joined Cochlear in 2000 and has a wealth of experience across the Company in roles including SVP, Manufacturing and Logistics and President, Asia Pacific. Prior to joining Cochlear, Dig worked for Boral and Boston Consulting Group.

4. Jan Janssen

*Senior Vice President, Design
and Development, Clinical
and Regulatory*

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

Senior Executive Team — continued

where he was involved in R&D in the fields of high-tech electronics and cochlear implants. Jan was promoted to Senior Vice President, Design and Development in 2005. Since August 2013, Jan has also had responsibility for Clinical and Regulatory.

5. Amanda Lampe

Senior Vice President, Corporate Affairs, Strategic Alignment & Public Health
BPE, GAICD

Amanda joined Cochlear in 2014. Previously held the role of SVP, Global Marketing in Cochlear. Has extensive senior management experience in government and corporate sectors. Previous experience includes ASX Group Executive for Corporate Affairs and Government Relations, chief of staff for a former Prime Minister and media director for a former NSW Premier.

6. Tony Manna

President, Americas Region
BS EET

Tony joined Cochlear in 2005. Has over 30 years medical device experience, including senior commercial

management roles at BEI Medical and Gyrus Medical. Prior roles in Cochlear include VP, Sales USA, General Manager, Cochlear Bone Anchored Solutions, USA and President, Cochlear Bone Anchored Solutions, Sweden.

7. Katharine McLennan

Senior Vice President, People & Culture
BS Biology (Hons), History (Hons), MBA, MA Political Science

Katharine joined Cochlear in March 2016 with experience in corporate strategy, talent and leadership development, and executive psychotherapy. Katharine has held leadership roles in Booz & Co, QBE Insurance and Commonwealth Bank of Australia.

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. He is a director of Osprey Medical Inc., President of the Group of 100 and a member of the Board of Taxation.

9. Stuart (Stu) Sayers

President, Services
BEC (Hons), MBA

Stu was appointed as Cochlear's inaugural President, Services in May 2016. The Services business provides aftercare services for Cochlear recipients and professionals, generating revenue from post-implant products and other offerings.

Stu comes with a wealth of experience in establishing and building customer-focused B2C and B2B service businesses, online and at scale. Most recently, Stu led the Amazon subsidiary Audible in Asia Pacific. Prior to Amazon, Stu ran E*TRADE and then Yahoo!7 in Australia and New Zealand. He previously held senior roles with Procter & Gamble and McKinsey & Company.

10. Dr Richard (Rich) Toselli

Chief Medical Officer

BA Biology, MD, MBA

Rich was appointed as Cochlear's inaugural Chief Medical Officer in June 2016. Rich will lead the Global Clinical, Regulatory and Health Economics teams to bring more strategic global coordination and integration. His focus will be on bringing stronger voice of customer to the product development process and sharpening the value proposition on our products by creating high quality clinical and health economic data.

Rich joined Cochlear from Sanofi Genzyme Biologics Division where he was Head of Global Medical Affairs for Immunology. Rich trained as a neurosurgeon and has more than 12 years of experience in R&D, medical affairs and evidence based medicine. He previously held senior roles with Sanofi, Covidien and Johnson & Johnson.

Financial Report

Cochlear Limited ACN 002 618 073 and its controlled entities for the year ended 30 June 2016

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The directors present their report, together with the Consolidated Financial Report of the Consolidated Entity (Cochlear), being Cochlear Limited (the Company) and its controlled entities, for the year ended 30 June 2016, and the Auditor's Report thereon.

Directors

The directors of the Company at any time during or since the end of the financial year were Mr R Holliday-Smith (Chairman), Mrs YA Allen, Mr G Boreham, AM, Prof E Byrne, AC, Ms A Deans, Mr A Denver, Mr DP O'Dwyer, Dr CG Roberts and Mr C Smith.

Information on the directors is presented in the Annual Report. This information includes the qualifications, experience and special responsibilities of each director. It also gives details of the directors' other directorships. Information on the Company Secretary including his qualifications and experience is presented in the Annual Report.

Directors' meetings

The number of directors' meetings (including meetings of committees of directors) and number of meetings attended by each of the directors of the Company during the financial year are:

	Board of directors		Audit Committee		People & Culture Committee		Medical Science Committee		Nomination Committee		Technology and Innovation Committee	
	Held	Attended	Held	Attended	Held	Attended	Held	Attended	Held	Attended	Held	Attended
Mr R Holliday-Smith	9	9	5	5	4	4	-	-	2	2	-	-
Mrs YA Allen	9	9	5	5	4	4	-	-	2	2	2	1
Mr G Boreham, AM	9	9	5	5	4	4	-	-	2	2	2	1
Prof E Byrne, AC	9	9	-	-	-	-	4	4	2	2	2	1
Ms A Deans	9	9	4	4	3	3	-	-	2	2	2	2
Mr A Denver	9	9	5	5	-	-	4	4	2	2	2	2
Mr DP O'Dwyer	9	9	5	5	-	-	4	4	2	2	2	2
Dr CG Roberts ¹	2	2	-	-	-	-	1	1	-	-	1	1
Mr C Smith ²	7	7	-	-	-	-	3	3	-	-	1	1

1. Dr CG Roberts retired 31 August 2015.

2. Mr C Smith was appointed on 1 September 2015.

Principal activities and review of operations and results

Operations

Business model

Cochlear's implant systems comprise an implant which is inserted during surgery and an external sound processor. This external sound processor can be upgraded with new technology as it becomes available.

Cochlear estimates that over 450,000 recipients have been implanted with one of its implants. Cochlear's business model includes supporting its customers with innovative and compatible products, through the sale of sound processor upgrades and accessories and ongoing product support.

Cochlear aims to remain the market leader in implantable hearing solutions. There is no independent published market share data but Cochlear estimates it has a market leading share of implantable hearing solutions.

Cochlear's global headquarters is based on the Macquarie University campus in Sydney, Australia. At this location are the corporate offices, manufacturing, research and development as well as the Asia Pacific regional headquarters.

Cochlear manages its sales and distribution through three geographical regions. There are several principal regional head offices plus many local offices:

- Americas, which includes the United States (US), Canada and Latin America;
- EMEA, which includes Europe, Middle East and Africa; and
- Asia Pacific, which includes Australasia and Asia.

Cochlear has a deep geographical reach, selling in over 100 countries. Cochlear has a direct presence in over 20 countries and uses distributors and agents in other areas.

Manufacturing for the cochlear implant product range is based in Australia, at three sites: Lane Cove and Macquarie University, in Sydney, and Brisbane. Lane Cove continues to manufacture Cochlear's legacy products. New implant ranges are manufactured at Cochlear's Macquarie University headquarters including the Nucleus Profile implant. The Brisbane site is responsible for manufacturing non-implant components.

The bone conduction implant product range is manufactured in Sweden.

The acoustic implant product range is manufactured across sites in Australia, the US and Belgium.

Cochlear's supply chain operates with product being distributed from its manufacturing sites in Australia and Sweden to its regional distribution centres in the US, the United Kingdom (UK) and Panama. The product is then further distributed to the end customer.

Cochlear's mission

We help people hear and be heard.

We **empower** people to connect with others and live a full life.

We **transform** the way people understand and treat hearing loss.

We **innovate** and bring to market a range of implantable hearing solutions that deliver a lifetime of hearing outcomes.

Strategic priorities

The hearing loss market offers an incredible business opportunity with over 360 million people worldwide experiencing disabling hearing loss, with nearly one in three people over the age of 65 affected by hearing loss.

With global market penetration for implantable hearing solutions being at less than 5%, there remains a significant, unmet and addressable clinical need that will continue to underpin the long-term sustainable growth of the business.

Cochlear's priorities will be centred on the customer with activities aimed at growing awareness and access to the industry for implant candidates. And with a growing recipient base, now numbering over 450,000, the Company is actively strengthening its servicing capability to provide products, programs and services to support the lifetime relationship with recipients.

Cochlear will continue with its commitment to being the technology leader in the industry by investing in research and development to improve hearing outcomes and expand the indications for implantable solutions so recipients can have the quality of life they expect.

Priorities are centred on four strategic platforms for the business:

1. Grow the core business

Implantable hearing devices will continue to be the driver of growth for the coming years. The focus will be to:

- **Strengthen the technology leadership position.** Over the next 18 months, there are plans to launch a series of new products across all categories of the business focused on both share and market growth;
- **Stimulate market growth** by increasing awareness of hearing loss. Over the last two years, Cochlear has developed a direct-to-consumer marketing strategy in the US to target potential candidates, follow up leads and nurture candidates through the channel. These learnings are now being taken to other countries;
- **Improve access for candidates** by expanding the cochlear implant clinic base as well as continuing to work with the referral channel to assist clinic partners to grow and become more efficient. The development of hybrid and acoustic implants, together with a broader range of electrodes, plays an important role in broadening the indications for implantable hearing solutions; and
- **Business model innovation.** Exploring new referral pathways and servicing models and where appropriate open company-owned Cochlear clinics to manage the aftercare of recipients.

2. Build a service business

With an ever growing base of recipients, now totalling over 450,000, Cochlear has both a lifetime responsibility and a significant business opportunity to service these recipients with upgrades and services that improve their quality of life by improving hearing performance. Cochlear will:

- **Support the growing recipient base** with upgrades, accessories and seamless service and repair;
- **Increase connectivity** and engagement with recipients with enhanced digital services; and
- **Introduce technology solutions for clinicians** to help clinic partners grow and make aftercare for recipients seamless.

3. Shape the organisation

Cochlear is reshaping the organisation to better-utilise and deploy resources. The focus is to:

- **Expand the Company's presence in customer facing activities** across developed markets by expanding the field force and marketing activities to be closer to customers and clinic partners. Cochlear will also increase its presence in emerging markets like China;
- **Globally integrate enabling activities** such as information technology (IT) to drive efficiencies and leverage best practice to fund market growth activities; and
- **Build organisational capabilities** to support customer-focused activities.

4. Value creation

To deliver long-term sustainable growth, Cochlear will:

- **Develop alliances and partnerships**, like the Smart Hearing Alliance with GN ReSound, which enables the Company to leverage its technology and leadership position to either expand the market or fast track growth.

Operating result FY16

Product highlights

	2016 \$000	2015 \$000	Change %	Constant currency
Cochlear implants (units)	30,172	26,838	↑ 12%	
<i>Sales revenue</i>				
Cochlear implants	729,171	604,346	↑ 21%	↑ 10%
Services (sound processor upgrades and accessories)	289,418	222,458	↑ 30%	↑ 20%
Acoustics (bone conduction and acoustic implants)	139,542	115,096	↑ 21%	↑ 9%
Total sales revenue	1,158,131	941,900	↑ 23%	↑ 12%

Cochlear implants – 63% of sales revenue

Cochlear implant revenue grew 21% (10% in constant currency) and unit sales grew 12% (8% excluding the benefit of China tender units) with solid growth experienced across developed and emerging markets. Leading developed markets, including the US, UK, Germany and Australia, all grew implant units by around 10%. Emerging markets performed well with highlights including strong growth in China, both in the private pay and tender markets, India and the Middle East.

There has been a strong uptake of the Nucleus Profile implants since release in FY15. The Profile series are the most reliable implants on the market and feature the world's thinnest electrodes, allowing for a reduction in surgery time and a less traumatic insertion. The Profile series implants are providing recipients with significant improvements in hearing performance in challenging listening situations when used with True Wireless accessories¹.

During the second half of FY16, we commenced a controlled market release of the new Slim Modiolar electrode (CI532) in Europe, the US and Canada. The CI532 is 60% thinner than the previous generation Contour Advance electrode, allowing for optimised surgical placement and an even less traumatic insertion.

Cochlear extended its sound processor portfolio during the second half with the introduction of Kanso. Kanso is a discrete, easy-to-use, off-the-ear sound processor that delivers the same hearing performance as the Nucleus 6 Sound Processor.

The increase in sales revenue also reflects earlier investments in sales and marketing capabilities including direct-to-consumer activities and field expansion across many markets. These initiatives help build awareness of implantable hearing solutions and support further penetration into the adult segment.

Services (sound processor upgrades and accessories) – 25% of sales revenue

Services sales revenue increased 30% (20% in constant currency) driven by the continuing strong uptake of the Nucleus 6 Sound Processor. With the launch of the Nucleus 6 for Nucleus 22 recipients, the latest sound processor is now compatible with all generations of implants released over the last 30 years.

Accessories growth was supported by the continued uptake of True Wireless and the Aqua+ for Nucleus 6 users.

Wireless Mini Microphone 2+, which streams speech directly to the Cochlear sound processor, was launched during the second half, providing further enhancements in hearing performance to the True Wireless range.

As part of the commitment to provide recipients with great customer experience, the business commenced the rollout of a number of service-oriented products. These products include the recipient membership program, Cochlear Family; a personalised online portal to connect recipients directly with Cochlear, MyCochlear.com; and Cochlear Link, which uses cloud based technology to provide recipients with simpler and faster servicing of their sound processors.

¹ Wolfe J, Morais M, Schafer E. Improving hearing performance for cochlear implant recipients with use of a digital, wireless, remote-microphone, audio-streaming accessory. J Am Acad Audiol. 2015 Jun;26(6):532-9.

Acoustics (bone conduction and acoustic implants) – 12% of sales revenue

Acoustics, which includes bone conduction and acoustic implant sales revenue, grew 21% (9% in constant currency) with solid performances across all regions. The bone conduction portfolio grew 10% in constant currency.

The Baha 5 portfolio was extended during the second half with the launch of Baha 5 Power and Baha 5 SuperPower Sound Processors, designed for recipients with higher degrees of hearing loss.

The Baha 5 System now provides the widest range of sound processors, including the industry's smallest, smartest and most powerful head-worn bone conduction solutions for those with single-sided deafness or who have conductive or mixed hearing loss. The Baha 5 System is also the only hearing implant system with MFi (made for iPhone) capabilities, allowing direct streaming between the sound processor and iPhones.

The Baha 5 Power and SuperPower Sound Processors are now commercially available in most key markets. They will be made available in other markets over the next 12 months as regulatory approvals are obtained.

Regional review

Sales revenue	2016 \$000	2015 \$000	Change %	Constant currency
Americas	519,688	402,962	↑ 29%	↑ 12%
EMEA (Europe, Middle East and Africa)	427,896	377,633	↑ 13%	↑ 7%
Asia Pacific	210,547	161,305	↑ 31%	↑ 23%
Total sales revenue	1,158,131	941,900	↑ 23%	↑ 12%

Americas (US, Canada and Latin America) – 45% of sales revenue

Sales revenue increased 29% to \$519.7 million (12% in constant currency). The highlight was the growth in the US with revenue growth of 16% in constant currency and cochlear implant unit sales up around 10%. Growth overall has been driven by new product introductions and growing services revenue, supported by strategic growth initiatives commenced over the past few years.

The expanded field sales organisation, direct-to-consumer marketing and new customer relationship management system (Salesforce.com) have supported accelerated market growth.

Services revenue increased by over 20% in constant currency driven by upgrades to the Nucleus 6 Sound Processor. The uptake by Nucleus 22 recipients has been enthusiastic since launch in November 2015.

Overall Latin American sales revenue declined in constant currency as a result of deteriorating economic conditions.

EMEA (Europe, Middle East and Africa) – 37% of sales revenue

Sales revenue increased 13% to \$427.9 million (7% in constant currency) with solid performances across the whole region.

The highlight was the performance of Germany, the largest market in EMEA, which grew units by around 10%. The German result reflects the impact of an expanded field sales team and investment in direct-to-consumer marketing activities.

Other key markets in Western Europe, particularly the UK and France, performed well with units also growing around 10% driven by investments in market growth initiatives and the positive impact of a strong product portfolio across all product categories.

Despite a challenging political and macro-economic year, sales revenue in the Middle East grew strongly, coming off a low base in FY15. The Middle East is benefiting from Cochlear's expanded presence since the opening of a new Middle East headquarters in Dubai in 2014. A headquarters was established in Vienna to service Central and Eastern Europe in April 2016.

Asia Pacific (Australasia and Asia) – 18% of sales revenue

Sales revenue increased 31% to \$210.5 million (23% in constant currency) with solid growth experienced across most markets.

Australia continues to grow consistently with unit growth of around 10% as the combination of field sales expansion and new marketing programs contributes to growing awareness.

China performed strongly in both the private pay and tender markets. Private pay sales and services revenue were boosted by the expansion of Cochlear's field sales presence. The region benefited from Chinese Central Government tenders of around 3,300 units.

India represents a small but rapidly growing market. The growing number of clinics, expansion of the field force and improvements in reimbursement all contributed to double-digit unit growth.

Financial review
Major expenses

	2016	2015	Change
	\$000	\$000	\$000
Cost of goods sold	333,593	275,320	58,273
<i>% of sales revenue</i>	<i>28.8%</i>	<i>29.2%</i>	<i>(0.4%)</i>
Selling and general expenses	326,090	260,809	65,281
Administration expenses	79,287	59,536	19,751
Research and development expenses	143,134	127,985	15,149
<i>% of sales revenue</i>	<i>12.4%</i>	<i>13.6%</i>	<i>(1.2%)</i>
Other income	(14,156)	(4,428)	(9,728)
EBIT	262,604	206,408	56,196
<i>% of total revenue</i>	<i>23.2%</i>	<i>22.3%</i>	<i>0.9%</i>

EBIT increased by \$56.2 million, up 27%, to \$262.6 million, with the operating margin (EBIT to total revenue) increasing by 0.9% to 23.2%.

Cost of goods sold (COGS) increased \$58.3 million to \$333.6 million, primarily as a result of growing volumes. COGS as a percentage of sales revenue improved by 0.4% to 28.8%, reflecting the impact of changes in foreign exchange (FX) rates, product and geographic mix as well as the higher COGS associated with the initial introduction of the Nucleus Profile series implant.

A balance sheet review was conducted in the context of new generation products launched over the past 18 months. This review has contributed to a \$16.3 million non-cash inventory write-off, pre tax, reflecting old and obsolete parts and products.

Selling and general expenses increased by \$65.3 million to \$326.1 million. The 25% increase reflects the increased investment in market growth initiatives as well as the impact on translation of the depreciation of the Australian dollar. In constant currency, the increase in selling and general expenses was 15%.

Administration expenses increased by \$19.8 million to \$79.3 million, an increase of 33%. More than half of the increase is related to investments in IT systems. The investment in global IT platforms will enable the business to strengthen its sales processes and build upon its services offering.

Investment in research and development (R&D) increased 12% to \$143.1 million, which is consistent with Cochlear's stated commitment to continue to invest in R&D to strengthen its technology leadership position. It follows several years of limited incremental investment in R&D.

Other income increased by \$9.7 million. A \$7.5 million increase in FX gains on asset translation is included in this line item.

Foreign currency impacts on the income statement

Income statement impacts	\$000
Reported FX contract gains/(losses) on hedged sales (transaction impact)	
- FX losses – FY16	(27,579)
- FX losses – FY15	(16,270)
	(11,309)
Sales revenue and expenses (translation impact) ¹	
- Sales revenue	93,467
- Total expenses including tax	(44,688)
	48,779
Reported asset translation impacts (translation impact)	
- FX gain on asset translation – FY16	8,695
- FX gain on asset translation – FY15	1,178
	7,517

1. FY16 actual v FY15 at FY16 rates.

Transaction impacts

Cochlear utilises currency hedging to provide some certainty around near-term cash flow. Over 90% of revenue and around 50% of costs are denominated in foreign currency. Most of the cash that is generated is repatriated to Australia to fund operating and investing activities, including R&D and dividends. In order to provide some certainty around near-term cash flow, expected cash flows are hedged back to Australian dollars (AUD).

In FY16, the AUD depreciated against most of the major currencies. As a result, FX losses on hedged sales were \$28 million. This compared to FX losses on hedged sales of \$16 million in FY15.

Translation impacts

The key translation impacts from translating foreign sales and expenses into AUD include:

- a net benefit to sales revenue of \$93.5 million;
- a net increase in expenses of \$44.7 million; and
- a net benefit to net profit of \$8.7 million from the translation of assets, primarily trade receivables. This compares to a \$1.2 million net benefit in FY15.

Capital employed

	2016	2015	Change
	\$000	\$000	\$000
Trade receivables	268,538	236,728	31,810
Inventories	154,103	145,861	8,242
Less: Trade and other payables	(110,354)	(99,858)	(10,496)
Working capital	312,287	282,731	29,556
<i>Debtor days</i>	85	83	2
<i>Inventory days</i>	169	193	(24)
Property, plant and equipment	86,878	80,809	6,069
Intangible assets	224,338	228,531	(4,193)
Other net liabilities	(57,125)	(96,182)	39,057
Capital employed	566,378	495,889	70,489

Capital employed increased by \$70.5 million to \$566.4 million since 30 June 2015 primarily as a result of an increase in working capital and a reduction in other net liabilities.

Working capital increased by \$29.6 million to \$312.3 million largely reflecting increased sales.

Trade receivables increased \$31.8 million to \$268.5 million. In constant currency, trade receivables increased by 11%, reflecting sales growth during the year. Debtors days increased by two days to 85 days.

Inventories increased \$8.2 million to \$154.1 million. Inventory days reduced 24 days to 169 days, reflecting the reduction in stock which had been built up in June 2015 ahead of tender shipments made during the first half and the higher sales, as well as the \$16.3 million inventory write off (as detailed in the prior major expenses commentary).

Net property, plant and equipment remained largely unchanged.

Intangible assets decreased by \$4.2 million to \$224.3 million, largely a result of revaluation to period end FX rates. All intangible assets are tested for impairment on an annual basis. There were no impairments or write-downs of intangible assets in FY16.

Other net liabilities reduced by \$39.0 million, largely reflecting higher tax payments made during the year.

Cash flow

	2016	2015	Change
	\$000	\$000	\$000
EBIT	262,604	206,408	56,196
Depreciation and amortisation	33,491	30,252	3,239
Changes in working capital and other	(20,006)	(8,418)	(11,588)
Net interest paid	(10,291)	(7,330)	(2,961)
Income taxes paid	(80,685)	(32,211)	(48,474)
Operating cash flow	185,113	188,701	(3,588)
Capital expenditure	(28,858)	(23,897)	(4,961)
Other investments	(21,276)	(4,530)	(16,746)
Free cash flow	134,979	160,274	(25,295)

The business generated strong cash flow with cash realisation of operating cash flow approximately equating to net profit.

An increase in EBIT of \$56.2 million was offset by a \$48.5 million increase in income taxes paid and a net \$11.5 million investment in working capital and other to fund business growth.

Income taxes paid increased by \$48.5 million, reflecting improved profitability and \$18.1 million of timing related payments following a change in the timing of Australian tax instalment payments. The effective tax rate has remained at approximately 26%. Further details are included in the 2016 Tax Contribution report which is available at the Investor Centre of the website, www.cochlear.com.

Net debt

	2016	2015	Change
	\$000	\$000	\$000
Loans and borrowings:			
Current	3,978	168,159	(164,181)
Non-current	189,260	44,552	144,708
Total debt	193,238	212,711	(19,473)
Cash and cash equivalents	(75,417)	(72,208)	(3,209)
Net debt	117,821	140,503	(22,682)
Total loan facilities	350,000	350,000	
Unused portion of debt facilities	155,000	135,000	

Net debt reduced by \$22.6 million to \$117.9 million since 30 June 2015. During FY16, the \$250 million debt facility was renewed for a further three years at lower interest rates.

At 30 June 2016, there was \$350.0 million in total loan facilities and the unused portion of the bank facility was \$155.0 million.

Dividends

	2016	2015	Change %
Interim ordinary dividend (dollars per share)	\$1.10	\$0.90	22%
Franking %	100%	35%	
Final ordinary dividend (dollars per share)	\$1.20	\$1.00	20%
Franking %	100%	100%	
Total ordinary dividends (dollars per share)	\$2.30	\$1.90	21%
Payout ratio %	70%	74%	
Franking %	100%	69%	

Strong free cash flow and the continued strength of the balance sheet have supported the payment of a final dividend of \$1.20 per share, franked at 100%. Total fully franked dividends of \$2.30 per share were declared for the year, an increase of 21% on dividends paid last year, representing a payout of 70% of net profit.

The record date for determining dividend entitlements is 8 September 2016 and the final dividend will be paid on 29 September 2016.

2017 financial outlook

For FY17, net profit is expected to be within a range of \$210-225 million, an increase of around 10-20% on FY16. Cochlear expects positive momentum to continue, with investments made in product development and market growth initiatives expected to underpin growth for FY17.

Key considerations for FY17:

- expect continued strong uptake of the Nucleus 6 and Kanso sound processors over the next few years with the current penetration rate for the Nucleus 6 at around 25% of potential recipients;
- Chinese Central Government tender units expected to be at similar levels to FY16 with delivery of units biased to the first half;
- in Europe, Cochlear does not expect any immediate impact on the business from the UK's decision to withdraw from the European Union. However, the Company remains alert to the potential for uncertainty to curtail economic growth and put pressure on health budgets;
- expect FY17 R&D expenditure to be broadly in line with that for FY16, representing a lower percentage of sales revenue;
- forecasting a weighted average AUD/USD FX rate of 75 cents for FY17 versus 73 cents in FY16; and
- the balance sheet position and free cash flow generation remain strong. The Company will continue to target a dividend payout ratio of around 70% of net profit.

Non-International Financial Reporting Standards (IFRS) financial measures

Given the significance of 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:

- Constant currency: restatement of IFRS financial measures in comparative years using FY16 FX rates.

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

Forward looking statements

Cochlear advises that this document contains forward looking statements which may be subject to significant uncertainties outside of Cochlear's control.

No representation is made as to the accuracy or reliability of forward looking statements or the assumptions on which they are based.

Actual future events may vary from these forward looking statements and it is cautioned that undue reliance not be placed on any forward looking statement.

Business risks

Cochlear has a sound and robust Risk Management Framework to identify, assess and appropriately manage risks. Details of Cochlear's Risk Management Framework can be found in the Corporate Governance Statement 2016 which is available at the Investor Centre on the website (www.cochlear.com).

Cochlear's principal business risks are outlined below. These are significant risks that may materially adversely affect Cochlear's business strategy, financial position or future performance. It is not possible to identify every risk that could affect Cochlear's business, and the actions taken to mitigate the risks described below cannot provide absolute assurance that a risk will not materialise.

Risk	Description and potential consequences	Strategies used by Cochlear to mitigate the risk
Product innovation and competition	Cochlear is exposed to the risk of failing to develop and produce innovative products for customers. Increased competition exposes Cochlear to the risk of losing market share as well as a decrease in average selling prices in the industry. Cochlear is also exposed to the risk of medical, biological and/or technological advancement by third parties where alternative products or treatments are developed and commercialised that render Cochlear's products obsolete. This could result in a loss of business.	In FY16, Cochlear invested around 12% of sales revenue in R&D. Cochlear also works with over 100 external research partners. The creation of new intellectual property and the protection of new and existing intellectual property are a key focus for Cochlear.

Risk	Description and potential consequences	Strategies used by Cochlear to mitigate the risk
Infringement litigation	Cochlear operates in an industry that has substantial intellectual property and patents, designs and trademarks protecting that intellectual property. Cochlear is exposed to the risk that it will be litigated against for claims of infringement. This could result in Cochlear paying penalties or royalties to be able to continue to manufacture product, or injunctions preventing Cochlear selling products it had developed.	Cochlear has a comprehensive patent portfolio across its technologies. Cochlear has a Legal department and utilises internal and external legal resources to deal with any litigation issues.
Misappropriation of know-how and intellectual property	Cochlear is exposed to the risk of its know-how and intellectual property being misappropriated either through hacking of its systems or by employees, consultants and others who from time to time have access to Cochlear's know-how and intellectual property. This could result in competitors using this information and increasing their competitiveness. Cochlear could lose market share as a result.	Cochlear monitors its systems and considers that it has appropriate safeguards and processes in place. Confidentiality agreements are in place with key employees and third parties that are exposed to Cochlear's know-how and intellectual property.
Regulation	Cochlear operates in a highly regulated industry. Medical devices are subject to strict regulations, including data security, of regulatory bodies in the US, Europe, Asia and Australia as well as many other local bodies in countries where Cochlear's products are sold. Regulatory bodies periodically perform audits at Cochlear's manufacturing sites. If Cochlear or a third-party supplier fails to satisfy regulatory requirements or the regulations change and modifications are not made, this could result in the imposition of sanctions or Cochlear's products being subject to recall and/or the loss of sales and reputational harm. Delays in achieving regulatory approval can impact Cochlear's ability to sell its latest technology.	Cochlear has a worldwide quality assurance system in place.
Reimbursement	The majority of Cochlear's customers rely on a level of reimbursement from insurers and government health authorities to fund their purchases. There is increasing pressure on healthcare budgets globally. Cochlear may also be subject to healthcare related taxes imposed by government agencies and this could negatively impact the ability of candidates to access Cochlear's products.	Cochlear continues to work with reimbursement and government agencies throughout the world to emphasise the benefits and cost effectiveness of the intervention.
Product liability	The manufacturing, testing, marketing and sale of Cochlear's products involve product liability risk. As the developer, manufacturer, marketer and distributor of certain products, Cochlear may be held liable for damages arising from use of its products during development or after the product has been approved for sale.	Cochlear maintains product liability insurance and operates a worldwide quality assurance system related to the design, testing and manufacture of its products.
Interruption to product supply	Cochlear relies on third-party suppliers for the supply of key materials and services. This carries the risk of delays and disruptions in supplies. Certain materials are available from a single source only and regulatory requirements make substitution costly, time-consuming or commercially unviable. Cochlear manufactures its latest generation products across six sites globally. There is the potential risk of disruption to sales should a manufacturing facility be unable to operate. Any new manufacturing facility will require regulatory approval prior to being able to produce and sell product from it. This approval could take many months.	Cochlear monitors its suppliers and identifies any available second-source supply. Inventories are managed and purchased in sufficient quantities for continued product supply in the short term. Where appropriate, lifetime buys, strategic raw materials purchases and supply chain interventions are made. Cochlear also regularly reviews its disaster recovery plans for its manufacturing sites.
Political, economic or social instability	Cochlear sells in over 100 countries. Several of the emerging markets are heavily biased to tender sales, including the Central Government of China's tenders. The future outcome of tender sales is uncertain. Regional political, economic or social instability could negatively impact sales and the receipt of payment for sales.	Cochlear assesses the countries it sells into and does not have a significant concentration of sales in countries impacted by political, economic or social instability. Cochlear utilises global scanning software to assess partners, distributors and suppliers against sanctions and police checklists on an ongoing basis. Cochlear reviews tenders carefully and participates at a level that makes commercial sense.

Risk	Description and potential consequences	Strategies used by Cochlear to mitigate the risk
FX rates	Cochlear is exposed to currency risk on sales and purchases that are denominated in a currency other than the respective functional currencies of the legal entities. The currencies in which these transactions primarily are denominated are Australian dollar (AUD), US dollar (USD), Euro (EUR), Japanese yen (JPY), Sterling, Swedish kroner (SEK) and Swiss francs (CHF). Over 90% of Cochlear's revenues and over 50% of costs are denominated in currencies other than AUD.	Currency risk is hedged in accordance with the Board approved treasury risk policy. The treasury risk policy aims to manage the impact of short-term fluctuations on Cochlear's earnings. Over the longer term, permanent changes in market rates will have an impact on earnings. Derivative financial instruments (forward exchange contracts) are used to hedge exposure to fluctuations in foreign exchange rates in a declining level of cover out to three years.
Credit	Cochlear's exposure to credit risk is influenced by the geographical location and characteristics of individual customers. Cochlear does not have a significant concentration of credit risk with a single customer. The majority of debtors are government supported clinics or major hospital chains.	Policies and procedures for credit management and administration of receivables are established and executed at a regional level. In monitoring customer credit risk, the ageing profile of total receivables balances and individually significant debtors is reported by geographic region to the Board on a monthly basis. Regional management is responsible for identifying high risk customers and placing potential restrictions on future trading, including suspending future shipments and administering dispatches on a prepayment basis. In addition, where appropriate, absolute country limits are in place and Chief Financial Officer approval is required to increase a limit. These limits are periodically reviewed by the Audit Committee.
Interest rates	Cochlear is exposed to interest rate risks in Australia.	Interest rate risk is hedged on a case-by-case basis by assessing the term of borrowings and the purpose for which the funds are obtained. Hedging against interest rate risk is achieved by entering into interest rate swaps. At 30 June 2016, no hedging had been entered into.
Operations	Operational risk is the risk of direct and indirect loss arising from a wide variety of causes associated with Cochlear's processes, personnel (including executive transitions), technology and infrastructure and generally accepted standards of corporate behaviour. Operational risks arise from all of Cochlear's operations. These risks could result in the loss of sales and reputational harm.	Standards for the management of operational risk are in place in the following areas: <ul style="list-style-type: none"> • requirements for appropriate segregation of duties, including the independent authorisation of transactions; • requirements for the reconciliation and monitoring of transactions; • documentation of controls and procedures; • requirements for the periodic assessment of operational risks faced, and the adequacy of controls and procedures to address the risks identified; • internal and external audit programs; • development of contingency plans; • succession planning for key management personnel; • training and professional development; • employee health and safety programs; and • ethical and business standards.

Consolidated results

The consolidated results for the financial year are:

	2016	2015
	\$000	\$000
Revenue	1,130,552	925,630
Profit before income tax	254,266	196,303
Net profit	188,921	145,840
Basic earnings per share (cents)	330.6	256.1
Diluted earnings per share (cents)	330.0	254.8

Dividends

Dividends paid or declared by the Company to members since the end of the previous financial year are:

	Dollars per share	Total amount \$000	Franked/unfranked	Date of payment
Interim 2016 ordinary	1.10	62,925	100% Franked	1 April 2016
Final 2015 ordinary	1.00	57,168	100% Franked	1 October 2015
Total amount	2.10	120,093		

Subsequent event

Since the end of the financial year, the directors declared the following dividends:

Final 2016 ordinary	1.20	68,646	100% Franked	29 September 2016
Total amount	1.20	68,646		

The financial effect of the 2016 final dividend will be recognised in the subsequent financial year as it was declared after 30 June 2016. Franked dividends paid or declared during the financial year were franked at the tax rate of 30% (2015: 30%).

Environmental regulations

Cochlear's operations are subject to environmental regulations under the Commonwealth of Australia and State/Territory legislation. The Board believes that Cochlear has adequate systems in place to manage its environmental obligations and is not aware of any breach of those environmental requirements as they apply to Cochlear.

Non-audit services

During the year, KPMG, the Company's auditor, performed certain other services in addition to its statutory duties. The Board has considered the non-audit services provided during the year by the auditor and in accordance with written advice provided by resolution of the Audit Committee, is satisfied that the provision of those non-audit services during the year by the auditor is compatible with, and did not compromise, the auditor independence requirements of the *Corporations Act 2001* for the following reasons:

- all non-audit services were subject to the corporate governance procedures adopted by the Company and have been reviewed by the Audit Committee to ensure that they do not impact the integrity and objectivity of the auditor; and
- the non-audit services provided do not undermine the general principles relating to auditor independence as set out in APES 110 Code of Ethics for Professional Accountants, as they did not involve reviewing or auditing the auditor's own work, acting in a management or decision-making capacity for the Company, acting as an advocate for the Company or jointly sharing risks and rewards.

Details of the amounts paid to the auditor of the Company, KPMG, and its related practices for audit and non-audit services during the year are set out below:

	Consolidated	
	2016	2015
	\$	\$
Audit services		
- audit and review of financial reports	1,583,831	1,559,738
- other regulatory compliance services	58,734	72,094
Total audit services	1,642,565	1,631,832
Non-audit services		
- taxation compliance and other services	1,051,398	988,156
Total non-audit services	1,051,398	988,156

State of affairs

There were no significant changes to the state of affairs of Cochlear during the financial year.

Remuneration Report

Contents

Section	Title	Description
1.	Introduction	Describes the scope of the Remuneration Report and the individuals whose remuneration details are disclosed. Outlines the link between performance and remuneration.
2.	Non-executive director remuneration	Provides details regarding the fees paid to non-executive directors.
3.	Executive remuneration	Details the remuneration provided to executives. Outlines the principles applied to executive remuneration decisions and the framework used to deliver the various components of remuneration.
4.	Employee share scheme and other share information	Provides details regarding Cochlear's employee equity plans including that information required by the <i>Corporations Act 2001</i> and applicable accounting standards.
5.	Remuneration governance	Describes the role of the Board and the People & Culture Committee, and the use of remuneration consultants when making remuneration decisions.

1. Introduction

Cochlear is a geographically diverse business, subject to rapid and changing competitive forces, including currency variations, and with a long history of growth. The Board remains committed to a strong growth focus and designs its executive remuneration strategies to direct behaviours towards achieving sustainable growth in shareholder value over the long term. Cochlear's policies must also be flexible enough to enable the Company to attract, motivate and retain high performing executives in many locations in a dynamic environment.

The Board's philosophy and approach to the remuneration of directors and executives are outlined in the Remuneration Policy, along with the role of the Board and the People & Culture Committee, and the use of remuneration consultants when making remuneration decisions. The Remuneration Policy is available in the Investor Centre/Corporate Governance/Company Policies section of our website (www.cochlear.com). This report refers to several other policies also available in the same section of the website.

During the year, the Board changed the name of the Human Resources Committee to the People & Culture Committee (P&CC) to better reflect the nature of the work of the P&CC, particularly in the context of the One Cochlear strategic initiative.

Our Chief Executive Officer/President (CEO/P) retired in FY16, and the role transitioned from Chris Roberts to Chris Smith on 1 September 2015 as Chief Executive Officer & President (CEO&P).

The Board believes Cochlear's approach to Board and executive remuneration remains balanced, fair and equitable and rewards and motivates a successful and experienced executive team to deliver ongoing business growth, which meets the expectations of shareholders over the long term.

1.1 Key management personnel

This Remuneration Report sets out, in accordance with the *Corporations Act 2001* and accounting standard requirements, the remuneration arrangements in place for key management personnel (KMP) of Cochlear during FY16.

KMP have authority and responsibility for planning, directing and controlling the activities of Cochlear and comprise the non-executive directors (NEDs), and executive KMP (being the senior executives named in this report, including the CEO&P who is an executive director). Details of the KMP during the year are set out in the table below:

	Title
Non-executive directors	
Rick Holliday-Smith	Chairman Chairman, Nomination Committee Member, Audit Committee, People & Culture Committee
Yasmin Allen	Director Chairman, Audit Committee Member, People & Culture Committee, Nomination Committee, Technology and Innovation Committee
Glen Boreham, AM	Director Chairman, People & Culture Committee Member, Audit Committee, Nomination Committee, Technology and Innovation Committee
Edward Byrne, AC	Director Chairman, Medical Science Committee Member, Nomination Committee, Technology and Innovation Committee
Alison Deans	Director Member, Audit Committee, People & Culture Committee, Nomination Committee, Technology and Innovation Committee
Andrew Denver	Director Chairman, Technology and Innovation Committee Member, Audit Committee, Medical Science Committee, Nomination Committee
Donal O'Dwyer	Director Member, Audit Committee, Medical Science Committee, Nomination Committee, Technology and Innovation Committee

Title	
Executive director	
Chris Roberts Retired 31 August 2015	Chief Executive Officer/President (CEO/P) Member, Medical Science Committee Member, Technology and Innovation Committee
Chris Smith Appointed 1 September 2015	Chief Executive Officer & President (CEO&P) Member, Medical Science Committee Member, Technology and Innovation Committee
Other executive KMP	
Richard Brook	President, European, Middle East and African Regions
Dig Howitt	President, Asia Pacific Region
Jan Janssen	Senior Vice President, Design and Development, Clinical and Regulatory
Neville Mitchell	Chief Financial Officer and Company Secretary
Tony Manna Appointed 1 July 2015	President, Americas Region

1.2 Relationship between Cochlear performance and executive KMP remuneration

1.2.1 Cochlear financial performance (FY11 to FY16)

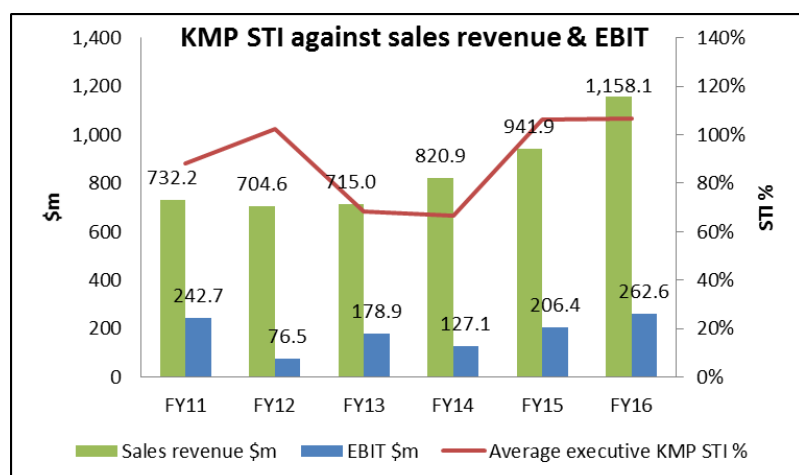
	FY11	FY12 ¹	FY13	FY14 ²	FY15	FY16
Sales revenue (\$million)	732.2	704.6	715.0	820.9	941.9	1,158.1
Earnings before interest and tax (EBIT) (\$million)	242.7	76.5	178.9	127.1	206.4	262.6
Net profit after tax (\$million)	180.1	56.8	132.6	93.7	145.8	188.9
Basic earnings per share (EPS) (cents)	318.2	100.0	233.0	164.6	256.1	330.6
EPS growth (3 years compound annual growth rate)	15.2%	-24.6%	-5.5%	-19.7%	36.8%	12.4%
Total dividend per share (\$)	2.25	2.45	2.52	2.54	1.90	2.30
Share price as at 30 June (\$)	72.00	65.84	61.71	61.70	80.15	121.25
Total shareholder return (TSR) (3 years)	70.8%	24.1%	-14.5%	-6.6%	41.7%	127.2%
TSR percentile ranking ³	96th	65th	28th	32nd	38th	94th

1. FY12 includes product recall expenses of \$138.8 million before tax and \$101.3 million after tax.
2. FY14 includes the patent dispute provision of \$22.5 million before tax and \$15.8 million after tax.
3. TSR ranking is shown over three financial years to 30 June. For long-term incentives performance is compared to TSR for ASX 100 companies.

For further explanation of details on Cochlear performance, see the Principal activities and review of operations and results section of the Directors' Report on pages 20 to 30.

1.2.2 Cochlear one year performance and relationship to executive KMP remuneration

Cochlear sales revenue grew 23% year on year. New product launches combined with investments in market growth initiatives drove this growth. EBIT in FY16 was 27% above that for FY15.



The short-term incentive (STI) payouts to executive KMP this year ranged from 97% to 112% of their target STI opportunity, reflecting the strong performance against targets and performance at expectations against personal objectives. Individual details are provided in table 3.2.

The payout ratios on STI in FY16 reflect individual, business and Cochlear performance against targets in accordance with plan rules. The Board has worked to ensure the overall executive KMP remuneration recognises Company performance and enables the business to retain a talented leadership team and allows Cochlear to promote internal candidates.

1.2.3 Cochlear three year performance and relationship to executive KMP remuneration

As explained in the Remuneration Policy (available on the website www.cochlear.com), Cochlear's remuneration framework aims to incentivise executive KMP towards long-term sustainable growth of the business and the creation of shareholder value in the short, medium and long term. The focus towards the longer term is developed in two ways:

- Equity STI, although dependent on sales revenue and EBIT performance and outcomes for the completed performance year (as explained in section 3.6) is deferred for a further two years; and
- Long-term incentive (LTI), in the form of options and performance rights, is linked to compound annual growth in EPS and relative TSR performance (as explained in section 3.6).

EPS growth (internal) and relative TSR (external) are generally accepted proxies for creation of shareholder value. The Board reviews the suitability of these performance criteria and settings on a regular basis to ensure they best serve shareholders' interests.

Earnings per share (EPS)

Vesting of the EPS portion of Cochlear executives' LTI over the last five years is displayed in the graphs below, overlaid with the compound annual growth rate (CAGR) of EPS for the corresponding performance period:

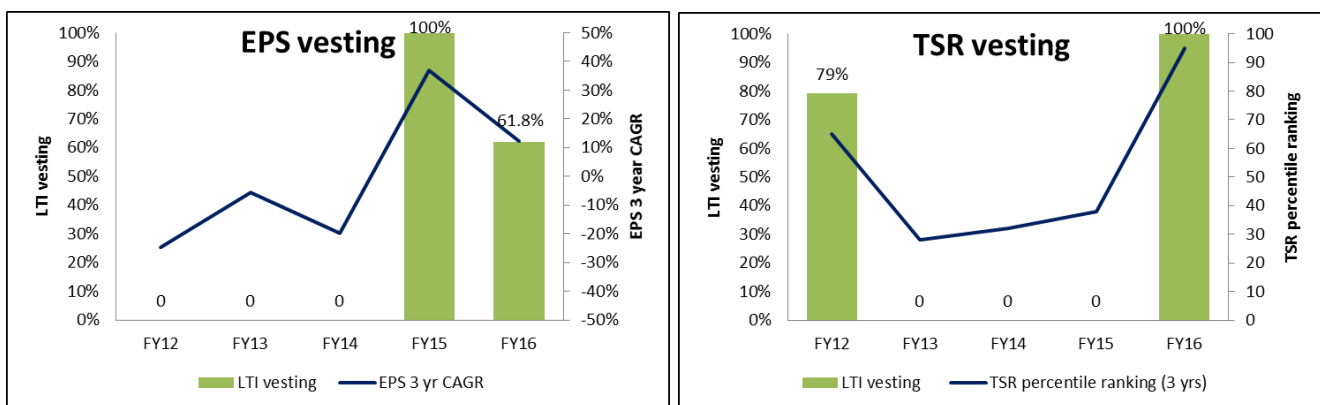
Cochlear's basic EPS in FY16 was 330.6 cents, which is a 12.4% compound annual growth rate (CAGR) over the three year vesting period. The vesting scale for our LTI plan generates 61.8% of the award at this growth level. This is the second time any part of the EPS portion has vested in the past five years. While this provides a strong alignment to shareholders' interests to grow EPS, the Board considers that the alignment is less strong if a lack of vesting results in executives not actually owning the shares that they are striving for.

Total shareholder return (TSR)

Cochlear's relative TSR performance over the relevant performance periods up to 30 June in respect of vested equity grants is displayed in the graphs below. This information was provided by an independent third party.

TSR is a function of share price growth and dividends reinvested. Cochlear's performance over time is affected by a range of variables, including currency volatility, global economic and geopolitical conditions, market growth for its products and variability in other sectors. The ASX 100 is biased towards high performance as lower performing companies drop out of the index and are replaced by growing companies.

Cochlear's TSR for the three years ended 30 June 2016 was ranked at the 94th percentile in the ASX 100. As a result, 100% of the TSR portion of the LTI has vested this year.



Vesting outcomes (performance shares/rights and options granted FY10 to FY14)

Grant date	Vesting date ¹	EPS 3 year CAGR ²	% vested ³	% forfeited ³	Relative 3 year TSR percentile ranking	% vested ³	% forfeited ³	Performance rights	Options	Net market value as at 30 June (\$) ⁴
								Market price as at 30 June (\$) ⁴	Exercise price (\$)	
17-Aug-09	Aug 2012	-24.6%	0.0%	100.0%	65th	79.3%	20.7%	65.84	60.04	5.80
16-Aug-10	Aug 2013	-5.5%	0.0%	100.0%	28th	0.0%	100.0%	N/A	69.80	N/A
15-Aug-11	Aug 2014	-19.7%	0.0%	100.0%	32nd	0.0%	100.0%	N/A	68.56	N/A
13-Aug-12	Aug 2015	36.8%	100.0%	0.0%	38th	0.0%	100.0%	80.15	62.78	17.37
15-Oct-13 ⁵	Aug 2016	12.4%	61.8%	38.2%	94th	100.0%	0.0%	121.25	59.13	62.12

1. While the vesting period ends on 30 June of each year, participants are not able to exercise any awards until the Board approves the opening of the first trading window under the Cochlear Trading Policy (typically immediately following the Cochlear full-year results announcement).

2. Compound annual growth rate.

3. All plan participants had the same vesting and forfeiture percentage outcome.

4. 30 June of applicable vesting date.

5. The performance hurdles for the LTI plans are considered demanding such that in the last four years, only 33% of allocations have vested.

1.2.4 Minimum shareholding guidelines

Executive KMP are requested to retain vested equity until they hold and maintain a holding of Cochlear shares equivalent to their annual salary in the previous year. The Board considers the minimum shareholding guideline to be best practice to strengthen the alignment of executives' interests to those of shareholders. New executives are likely to take some length of time to build such a holding if the LTI plan fails to vest as it has in recent times. With that in mind, the Board intends to review the performance hurdles for future LTI equity grants.

The table in section 4.4 details the current holdings of executive KMP.

1.3 Fee changes

Board fees must recognise the effort required to fulfil the responsibilities of the non-executive directors. Reflecting the increasing governance requirements, the work of the Board and its various committees has increased, and the Board considered it appropriate to revise committee fees for FY16. This is detailed in section 2.1 and base fees represent 74.0% of the \$2.5 million aggregate amount approved by shareholders at the October 2015 AGM.

The Board approved a 4.6% increase in total Board remuneration effective 1 July 2016. This increase will apply to base fees which have not changed since 2011.

2. Non-executive director remuneration

2.1 NED fees FY16

Board fees		Committee fees	FY16		FY15	
			Committee Chair	Committee member	Committee Chair	Committee member
Board Chairman fee ¹	\$438,000	Audit	\$50,000	\$25,000	\$40,000	\$20,000
Board NED base fee	\$146,000	People & Culture	\$30,000	\$15,000	\$30,000	\$10,000
		Medical Science	\$30,000	\$15,000	\$20,000	\$10,000
		Nomination	No fee	No fee	No fee	No fee
		Technology and Innovation	\$40,000	\$20,000	\$20,000	\$10,000

1. Committee fees are not paid to the Chairman of the Board.

2.2 Post-employment benefits and other policy items

Superannuation	Where required, superannuation contributions have been made in accordance with Australian superannuation legislation, at a rate of 9.5% of the base fee up to the Australian Government's prescribed maximum contributions limit. Contributions are not included in the base fee.
Retirement scheme	Prior to 2003, Cochlear operated a directors' retirement scheme which provided retirement benefits of three times their average annual remuneration over the previous three years. In 2006, the Board resolved to discontinue the ongoing accrual of benefits subject to a transition period to 2011. The benefits accrued are indexed by reference to the bank bill rate. At 30 June 2016, Edward Byrne is the only NED entitled to this benefit. The accrued entitlement for Edward Byrne under the Cochlear directors' retirement scheme as at 30 June 2016 was \$442,034.
Equity instruments	NEDs do not receive any performance related remuneration, options or performance shares/rights.
Other fees/benefits	NEDs receive reimbursement for costs directly related to Cochlear business.
Minimum shareholding guidelines	NEDs are requested to hold shares equivalent to the fees received in the previous 12 months. The Share Ownership Policy is available on the website.

2.3 NED total remuneration

Amounts \$	Year	Short-term	Post-employment		Total
		benefits	Accrued interest ¹	Superannuation benefits	
		Fees			
Rick Holliday-Smith (Chairman)	FY16	438,000	-	19,308	457,308
	FY15	438,000	-	18,783	456,783
Yasmin Allen	FY16	230,731	-	19,308	250,039
	FY15	196,000	-	17,986	213,986
Paul Bell ²	FY15	54,154	-	5,145	59,299
Glen Boreham ³	FY16	220,654	-	19,308	239,962
	FY15	85,969	-	8,167	94,136
Edward Byrne	FY16	195,846	9,586	18,248	223,680
	FY15	176,000	10,729	16,720	203,449
Alison Deans ³	FY16	192,154	-	18,255	210,409
	FY15	76,200	-	7,239	83,439
Andrew Denver	FY16	225,769	-	19,308	245,077
	FY15	196,000	-	17,986	213,986
Donal O'Dwyer	FY16	205,846	-	18,686	224,532
	FY15	186,000	-	17,547	203,547
Total⁴	FY16	1,709,000	9,586	132,421	1,851,007
	FY15	1,408,323	10,729	109,573	1,528,625

1. Amounts accrued for interest during the financial year relating to the directors' retirement scheme.

2. Retired 17 October 2014.

3. Appointed 1 January 2015.

4. The year-on-year changes in Board fees reflect the appointment of two additional directors half way through FY15 and loss of one, changes in Board committee membership and increases to committee fees. There have been no increases in Board NED base fees for four years.

The table below indicates Cochlear Limited shareholdings:

	Held at 1 July 2015	Purchases	Sales	Cochlear Limited ordinary shares held as at 30 June 2016	Total intrinsic value of Cochlear Limited securities as at year end (\$)¹
Rick Holliday-Smith	9,250	750	-	10,000	968,300
Yasmin Allen	3,500	-	-	3,500	338,905
Glen Boreham	-	2,800	-	2,800	271,124
Edward Byrne	3,250	-	-	3,250	314,698
Alison Deans	2,000	-	-	2,000	193,660
Andrew Denver	4,000	-	-	4,000	387,320
Donal O'Dwyer	6,000	-	-	6,000	580,980
Total	28,000	3,550	-	31,550	3,054,987

1. In line with the Share Ownership Policy (available on our website), the intrinsic value of Cochlear Limited ordinary shares is calculated using the average daily share price over the previous 12 months (\$96.83), as at closing on the ASX up to 30 June 2016, times the number of shares.

All NEDs are compliant with the Share Ownership Policy which allows an additional three year window to increase holdings where increased directors' committee responsibilities have resulted in increased fees.

3. Executive remuneration

3.1 Executive remuneration table – Audited statutory disclosure (accounting cost to Cochlear)

Year	Fixed remuneration				Variable remuneration				End of service	Total	Proportion of total remuneration			
	Amounts \$	Short-term	Other employee costs	Total	Short-term incentive (STI) ²	Long-term incentive (LTI) ^{6,7}	Total	Performance related						
Name	Salary	Non-monetary benefits ¹	Superannuation benefits	Long service leave	Cash STI and special incentive ³	Deferred STI ^{4,5}	Value of options	Value of performance shares/rights			%			
Chris Roberts ^{8,9}	FY16	609,526	-	9,654	-	619,180	204,759	32,056	80,829	-	317,644	-	936,824	33.9%
	FY15	1,431,029	-	18,783	32,349	1,482,161	1,338,462	518,549	1,055,244	-	2,912,255	1,548,418	5,942,834	49.0%
Chris Smith ^{9,10}	FY16	1,341,409	285,865	-	-	1,627,274	1,200,924	192,418	481,906	252,384	2,127,632	-	3,754,906	56.7%
	FY15	786,650	26,797	16,290	-	829,737	464,806	72,305	186,605	81,625	805,341	-	1,635,078	49.3%
Richard Brook	FY16	674,740	105,353	126,953	-	907,046	374,074	91,517	150,138	188,994	804,723	-	1,711,769	47.0%
	FY15	611,858	91,970	103,860	-	807,688	342,690	55,609	141,217	58,134	597,650	-	1,405,338	42.5%
Dig Howitt ¹¹	FY16	528,951	-	19,308	13,563	561,822	371,964	54,991	249,140	61,731	737,826	-	1,299,648	56.8%
	FY15	387,709	-	14,088	-	401,797	212,412	21,145	51,190	104,771	389,518	-	791,315	49.2%
Jan Janssen	FY16	552,032	-	19,308	(2,274)	569,066	348,992	79,795	140,048	162,097	730,932	-	1,299,998	56.2%
	FY15	515,161	-	18,783	6,416	540,360	311,250	46,396	115,591	85,174	558,411	-	1,098,771	50.8%
Tony Manna ¹²	FY16	585,992	26,073	22,451	-	634,516	335,386	32,039	56,921	18,284	442,630	-	1,077,146	41.1%
Neville Mitchell ¹³	FY16	583,293	-	191,351	27,680	802,324	435,969	98,370	147,082	223,846	905,267	-	1,707,591	53.0%
	FY15	543,609	-	157,325	17,325	718,259	381,709	56,973	78,902	168,892	686,476	-	1,404,735	48.9%
Mark Salmon ¹⁴	FY15	143,181	-	5,743	9,852	158,776	23,397	(15,737)	(10,692)	145,943	142,911	-	301,687	47.4%
Total	FY16	4,875,943	417,291	389,025	38,969	5,721,228	3,272,068	581,186	1,306,064	907,336	6,066,654	-	11,787,882	51.5%
	FY15	4,419,197	118,767	334,872	65,942	4,938,778	3,074,726	755,240	1,618,057	644,539	6,092,562	1,548,418	12,579,758	48.4%

- Benefits include housing allowances for expatriate KMP, car allowances and health insurance which are market based payments.
- STI and LTI are awarded annually, with cash incentives paid half yearly. The service and performance criteria are set out in this report.
- During the year the Board approved a Special Incentive program specific to the One Cochlear change initiative.
- Deferred STI is granted in performance rights and deferred for a further two years. The cost of the plan is expensed across three years. The FY16 amount represents the portion of the FY14, FY15 and FY16 deferred STI expensed in FY16. The FY15 amount represents the portion of the FY14 and FY15 deferred STI expensed in FY15. The Cochlear Executive Incentive Plan (CEIP) was introduced in FY14, so there was no FY13 grant to be included in the FY15 expense.
- FY15 deferred STI for Chris Roberts includes an expense of \$298,234 that would normally have been amortised over future years for awards that remain subject to vesting timeframes. FY15 also includes a credit of \$15,737 for Mark Salmon, reversing prior years' expenses on plans that have been forfeited.
- The value of options and performance shares/rights is calculated at the date of grant using the Black-Scholes-Merton pricing model discounted for vesting probabilities of non-market performance criteria. The value of options and performance shares/rights is allocated to each reporting period evenly over the period from grant date to vesting date. The amount expensed each reporting period includes adjustments to the life-to-date expense of grants based on the reassessed estimate of achieving non-market performance criteria and final vesting amounts for the non-market performance criteria of options and performance shares/rights. The value disclosed above is the portion of the value of the options and performance shares/rights recognised as an expense in the financial year. The ability to exercise the options and performance shares/rights is conditional on Cochlear achieving certain performance hurdles. Further details of options and performance rights granted during the financial year are set out in this report.
- FY15 includes an expense of \$391,834 for Chris Roberts and \$34,179 for Mark Salmon that would normally have been amortised over future years for awards that remain subject to vesting hurdles and timeframes and may not be paid out. Also includes a credit of \$46,401 for Mark Salmon, reversing prior years' expenses on plans that have been forfeited.
- FY15 included an accrual of contractual end of service payments of approximately one year of salary for Chris Roberts, payable at the end of his employment, and statutory entitlements to bring his total reward for FY15 to \$5,942,834. In FY16, Chris Roberts did not accrue any more end of service amounts.
- Chris Roberts was an executive director and retired on 31 August 2015. Chris Smith is an executive director in FY16.
- Chris Smith's remuneration increase reflects an increase in base salary due to his promotion to the CEO&P role, allowances due to his relocation to Sydney, overachievement on STI and currency variations.
- Dig Howitt became a KMP on 29 September 2014. Values in this table relate only to the period he was a KMP.
- Tony Manna became a KMP on 1 July 2015. Values in this table relate only to the period he was a KMP.
- Neville Mitchell remains on a transitional defined contribution superannuation plan based on a fixed percentage of base and STI.
- Mark Salmon retired on 26 September 2014.

3.2 Executive remuneration table - Unaudited

The table below aims to show actual remuneration received during the year including equity vesting from prior years, and separately to show actual remuneration granted during the year including equity deferred to future years:

Name	Year	Fixed remuneration and cash incentives received			Proportion of STI		Past at risk remuneration received during year			Actual remuneration received	Future at risk remuneration received	
		Fixed remuneration ¹	Special incentive ²	STI Cash Incentives ³	Achieved %	Forfeited %	Value of vested deferred STI	Intrinsic value of vested options ⁴	Intrinsic value of vested performance shares (LTI) ⁴		Deferred STI ⁵	LTI (equity) granted during year ⁶
Chris Roberts ⁷	FY16	619,180	-	204,759	108.1%	-	-	2,583,213	-	3,407,152	-	-
	FY15	1,449,812	-	1,338,462	120.0%	-	-	-	-	2,788,274	401,538	1,300,967
Chris Smith	FY16	1,627,274	-	1,200,924	107.7%	-	-	490,489	66,980	3,385,667	360,340	1,306,785
	FY15	829,737	-	464,806	109.4%	-	-	-	-	1,294,543	139,442	329,947
Richard Brook	FY16	907,046	15,000	359,074	96.8%	3.2%	-	469,399	-	1,750,519	107,722	328,759
	FY15	807,688	-	342,690	101.8%	-	-	-	-	1,150,378	102,807	249,928
Dig Howitt ⁸	FY16	548,259	33,500	338,464	112.0%	-	-	-	260,427	1,180,650	101,539	253,191
	FY15	401,797	-	212,412	97.9%	2.1%	-	-	-	614,209	63,724	234,804
Jan Janssen	FY16	571,340	15,000	333,992	106.1%	-	-	302,913	105,863	1,329,108	100,197	254,020
	FY15	533,944	-	311,250	106.6%	-	-	-	-	845,194	93,375	238,188
Tony Manna ⁹	FY16	634,516	15,000	320,386	108.7%	-	-	287,046	-	1,256,948	96,116	193,307
Neville Mitchell	FY16	774,644	22,000	413,969	107.3%	-	-	124,962	262,089	1,597,664	124,191	306,439
	FY15	700,934	-	381,709	106.8%	-	-	-	-	1,082,643	114,513	281,347
Mark Salmon ¹⁰	FY15	148,924	-	23,397	100.0%	-	-	-	-	172,321	-	-
Total	FY16	5,682,259	100,500	3,171,568	-	-	-	4,258,022	695,359	13,907,708	890,105	2,642,501
	FY15	4,872,836	-	3,074,726	-	-	-	-	-	7,947,562	915,399	2,635,181

1. Represents the value of base salary, non-monetary benefits and superannuation received during the year (excludes the accrued value of long service leave).
2. During the year the Board approved a Special Incentive program specific to the One Cochlear change initiative.
3. Represents STI payments earned during the financial year. For example, FY16 data includes first half STI payments received in February, and second half STI payments which are accrued at year end, and received in August 2016, after the reporting year end.
4. Reflects the intrinsic value of vested employee share scheme benefits at the date of exercise. In the case of options, this represents the market price on the date of exercise (or market price on date of vesting in the case of unvested options) less the exercise price multiplied by the number of options. For performance shares, this represents the share price on the date of exercise.
5. Deferred STI in FY16 reflects STI achievement of between 97% and 112% for performance in FY16.
6. Represents the value of equity grants (options and/or performance rights) calculated at the date of grant using the percentage of salary reflected in the remuneration mix. These grants were awarded during the year, are unvested and will be subject to achievement of future performance hurdles.
7. For FY15, Chris Roberts also received an end of service payment of \$1,548,418.
8. Dig Howitt became a KMP on 29 September 2014. Values included in this table relate only to the period he was a KMP. Both the deferred STI value (scheduled for conversion to performance rights in August 2017) and the LTI value (granted in October 2014) are included in full as they were granted after he became a KMP.
9. Tony Manna became a KMP on 1 July 2015.
10. Mark Salmon retired on 26 September 2014.

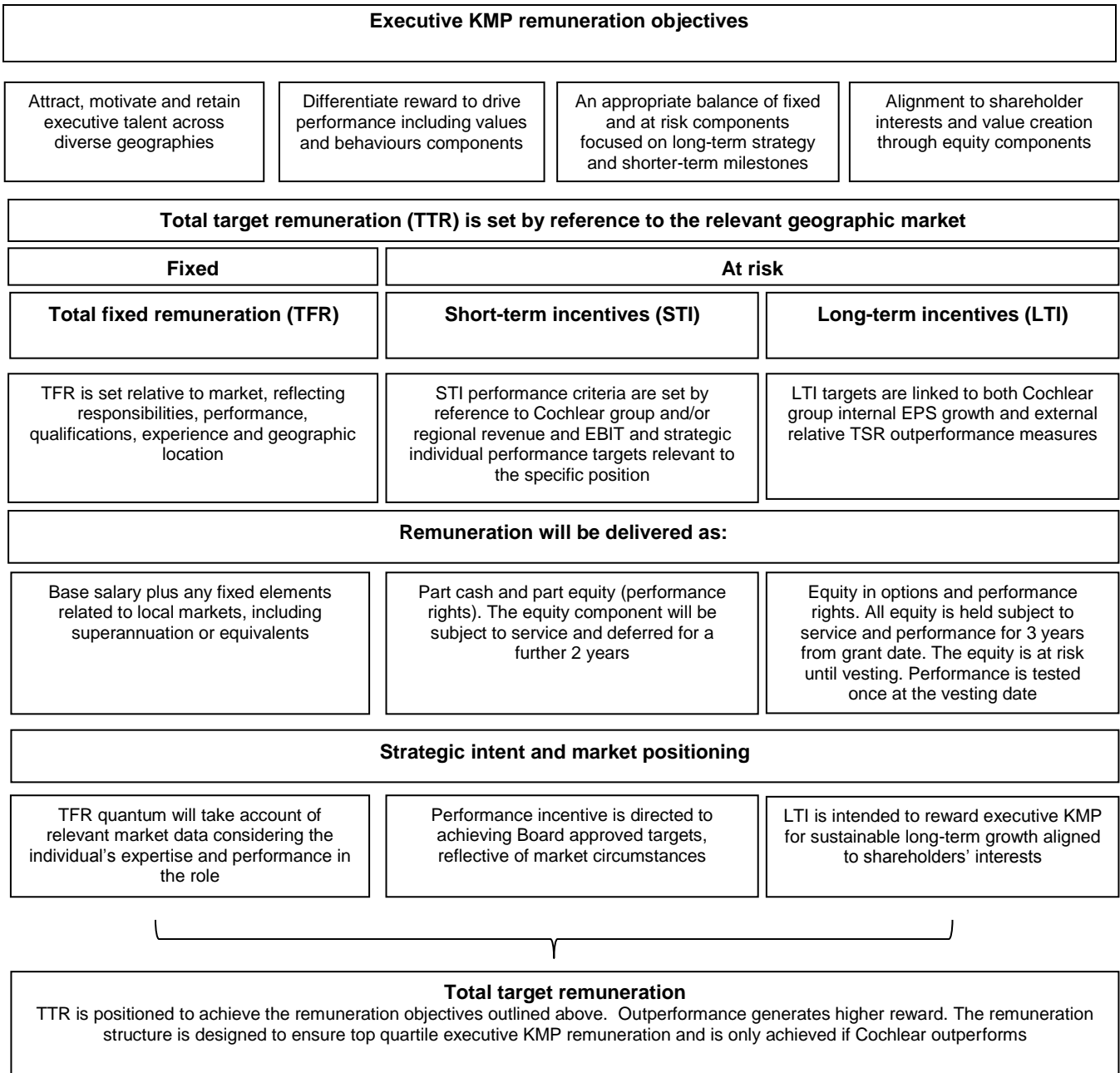
The table is not mandatory, and there is no prescribed approach to providing it. Our approach in FY16 has changed from FY15 as follows:

- Cochlear's STI is paid half yearly. In the FY15 report, the STI shown comprised the payments paid during the year i.e. August 2014 payment relating to second half performance FY14, and February 2015 payment relating to first half performance FY15. We believe shareholders are interested in the STI earned during the year. The FY16 approach adds the two half year performances for FY16. We have restated the FY15 numbers to include the February 2015 and the August 2015 payments; and
- in the FY15 report, the value disclosed for the LTI granted in the year and deferred to future years was calculated in accordance with IFRS-2. For FY16, we have shown the intended value of the grant under the remuneration framework (i.e. a percentage of base or fixed remuneration). We believe this simpler approach meets the needs of shareholders. We have restated the FY15 numbers to reflect this new approach.

3.3 Executive KMP remuneration

Cochlear's executive remuneration policies are designed to attract, motivate and retain a highly qualified and experienced group of executives employed across diverse geographies.

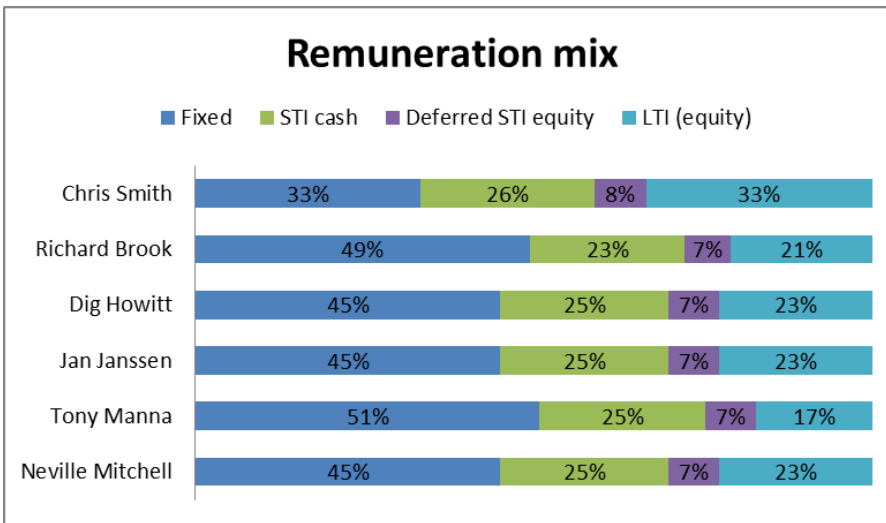
Executive KMP remuneration objectives are delivered through three categories of remuneration, as illustrated below:



3.4 Remuneration composition mix and timing of receipt

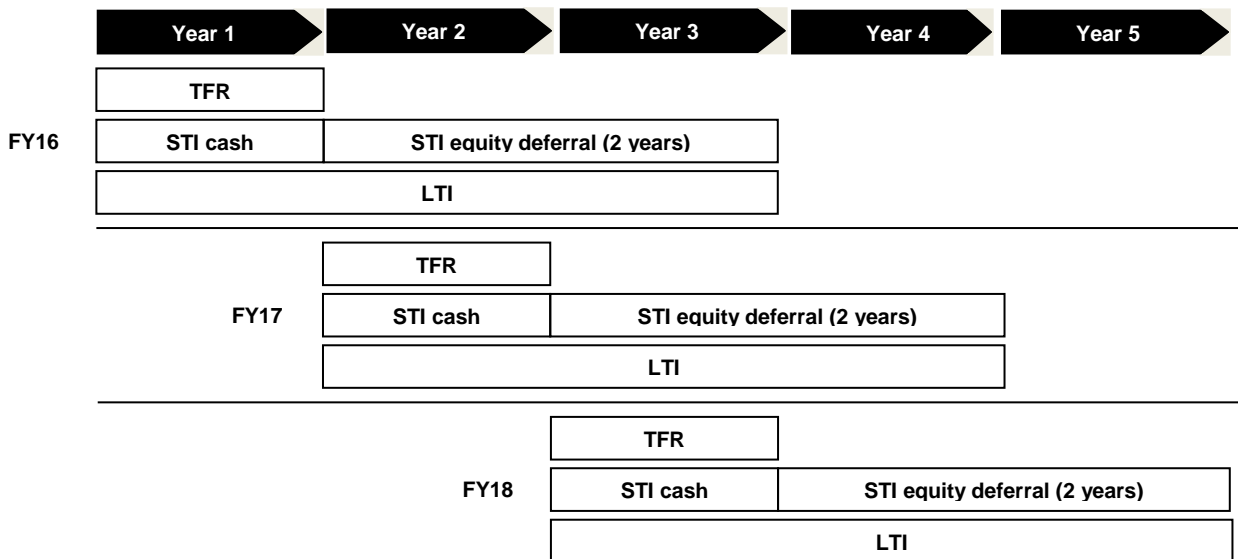
3.4.1 Current remuneration mix

Cochlear aims to provide an appropriate and competitive mix of remuneration components balanced between fixed and at risk and paid in both cash and deferred equity. The broad remuneration composition mix for executive KMP can be illustrated as follows:



3.4.2 Remuneration - Timing of receipt of remuneration

The three complementary components of executive KMP remuneration are earned over multiple time ranges. This is illustrated in the following chart:



Note: LTI is awarded in year 1 and earned at the end of year 3 but expensed over the three year service period.

As illustrated, executive KMP remuneration is delivered on a rolling basis, with a material component deferred for two (STI) and three (LTI) years and awarded as equity. This remuneration mix is designed to ensure executive KMP are focused on delivering results over the short, medium and long term if they are to maximise their remuneration opportunity. The Board believes this approach aligns executive KMP remuneration to shareholder interests and expectations.

3.5 Total fixed remuneration explained

Total fixed remuneration includes all remuneration and benefits paid to executive KMP calculated on a total employment cost basis. In addition to base salary, executives may receive benefits in line with local practice, such as health insurance, car allowances and relocation allowances. Retirement benefits are generally paid in line with local legislation and practice.

Executive KMP remuneration is tested regularly for market competitiveness by reference to appropriate independent and externally sourced comparable benchmark information, taking into account an executive's responsibilities, performance, qualifications, experience and geographic location. The review examines fixed and variable components separately and in totality. Any adjustments to executive KMP remuneration are approved by the Board, based on P&CC and CEO&P recommendations.

3.6 Variable (at risk) remuneration explained

As set out in section 3.4, variable remuneration forms a significant portion of executive KMP remuneration opportunity. Cochlear's performance hurdles are at the higher end of the "difficult to achieve" spectrum compared to market practice within ASX 100 companies. Apart from being market competitive, the purpose of variable remuneration is to direct executives' behaviours towards maximising Cochlear's short, medium and long-term performance. The key aspects are summarised below:

3.6.1 Short-term incentives (STI)

Purpose	<p>The STI arrangements at Cochlear are designed to reward executives for achievement against annual performance targets set by the Board at the beginning of the performance period. The STI program is reviewed annually by the P&CC and approved by the Board.</p> <p>All STI awards to executive KMP are approved by the P&CC and Board. The deferred STI is designed to encourage a longer-term focus, and ensure reward is linked to longer-term outcomes from shorter-term goals.</p>
Performance targets	<p>For FY16, 80% of STI was based on financial targets set by the Board and having regard to prior year performance, global market conditions, the competitive environment, future prospects and the Board approved budgets. The specific targets are not detailed in this report due to their commercial sensitivity.</p> <p>For FY16, two financial targets (sales revenue and EBIT) had equal weighting. The weighting between Cochlear group and regional financial goals depends on the responsibilities and scope of influence of the individual executive KMP.</p> <p>In FY16, individual performance goals accounted for a 20% weighting for executive KMP based on a range of strategic objectives determined each year.</p> <p>For FY17, the weighting will change to 60% financial and 40% One Cochlear goals. One Cochlear goals are specific to the individual and aligned to Cochlear's strategic priorities.</p>
Mandatory deferral of STI	<p>A mandatory deferral of a portion of STI (in the form of performance rights) is intended to reinforce alignment with shareholder interests. The deferred STI target is a percentage of base pay. Based on performance as measured under the (cash) STI plan, grants are calculated at the end of each year and then held for two years until vesting. This achieves additional retention and alignment of executives with longer-term shareholder interests.</p> <p>The number of performance rights is determined based on Black-Scholes-Merton valuations (without discounting for performance) using the Cochlear five day volume weighted average share price following the announcement of full-year results in August each year.</p> <p>Once the performance rights are awarded, there are no further performance measures other than continued tenure for the vesting period (two years).</p>

3.6.2 Long-term incentives (LTI)

The LTI provides an annual opportunity for executive KMP and other selected senior executives (based on their ability to influence and execute strategy) to receive an equity award deferred for three years. This is intended to align a significant portion of executives' overall remuneration to shareholder value over the longer term. All LTI awards remain at risk and subject to forfeiture or lapse until vesting and must meet or exceed target EPS growth rates and/or relative TSR performance hurdles over the vesting period.

Purpose	To align executive KMP remuneration opportunity with shareholder value and provide retention stimulus.
Types of equity awarded	<p>LTI up to FY13 was provided under the Cochlear Executive Long Term Incentive Plan (CELTIP). Previous reports have detailed that plan.</p> <p>The Cochlear Executive Incentive Plan (CEIP) was introduced in July 2013. See section 4.1 for further details.</p> <p>Under the CEIP, selected senior executives are offered options (being an option at a pre-set exercise price to acquire a fully paid ordinary share of Cochlear Limited) or performance rights (being a nil exercise price right to a fully paid ordinary share of Cochlear Limited). A minimum 30% of the LTI value must be taken as options. The share price at vesting must be greater than share price at grant in order for any reward to be delivered under the option program.</p>
Time of grant	All equity grants will be made after the AGM each year but based on values determined in the preceding August.
Time restrictions	Equity grants are tested against the performance hurdles set, at the end of three financial years. If the performance hurdles are not met at the vesting date, options and performance rights lapse.

Performance hurdles and vesting schedule	Equity grants to executive KMP are in two equal tranches assigned 50% to growth in EPS and 50% subject to relative TSR. The performance conditions applying to the latest grant (FY16) were as follows:			
	Compound annual growth rate in EPS (3 years)		Ranking of TSR against S&P/ASX 100 (3 years)	
	Performance	% of equity to vest	Performance	% of equity to vest
	< 10%	0%	< 50th percentile	0%
	10% to 20%	50% to 100% pro-rata	50th to 75th percentile	40% to 100% pro-rata
	> 20%	100%	> 75th percentile	100%
	Options and performance rights vest if the time restrictions and relevant performance hurdles are met. The Board must approve any special provisions, in accordance with Company policies, in the event of termination of employment or a change of control. Under the CEIP, after the three year vesting schedule, any vested options expire after seven months if they have not been exercised.			
Dividends	No dividends are attached to options or performance rights.			
Voting rights	There are no voting rights attached to options or performance rights.			
Retesting	There is no retesting of performance hurdles under the LTI plan.			
LTI allocation	<p>The size of individual LTI grants for executive KMP is determined in accordance with the Board approved remuneration strategy mix. See section 3.4.</p> <p>The target LTI dollar value for each executive is converted to options and performance rights according to LTI allocation values independently determined based on the gross contract value of the relevant equity instrument and based on a Black-Scholes-Merton pricing model without discounting for service or EPS and TSR performance hurdles:</p> <ul style="list-style-type: none"> option allocation = LTI dollar value/Black-Scholes-Merton value before service or EPS and TSR performance discounts; and/or performance right allocation = LTI dollar value/Black-Scholes-Merton value before service or EPS and TSR performance discounts. 			

3.7 Other remuneration elements and disclosures relevant to executive KMP

3.7.1 Minimum shareholding guidelines

In March 2007, the Board approved minimum shareholding guidelines for NEDs and executive KMP. All NEDs are requested to accumulate a minimum shareholding in Cochlear shares equivalent in value to the prior year's fees. NEDs have three years in which to build this requirement, and an additional three years if an increase is required resulting from increased committee responsibilities. All executive KMP are requested to accumulate a minimum shareholding in Cochlear shares or vested options equivalent to the prior year's total fixed remuneration. They are not required to purchase shares for this purpose, but are restricted from selling shares derived from vesting equity plan awards until they accumulate their minimum shareholding. The value of shareholdings for the purpose of these guidelines is based on the 365 day average Cochlear Limited closing share price for the prior year.

All NEDs and executive KMP are compliant with the share ownership guidelines. The guidelines are available on the Cochlear website.

3.7.2 Clawback

Cochlear implemented a Clawback Policy to take effect from 1 July 2014 to meet good governance practice. The policy is available on the Cochlear website. There have been no circumstances to date where the policy was invoked.

3.7.3 Hedging and margin lending prohibition

In line with good corporate governance, Cochlear has a formal policy setting down how and when employees of Cochlear may deal in Cochlear securities. Cochlear's Trading Policy is available on the Cochlear website.

Under the Cochlear Trading Policy and in accordance with the *Corporations Act 2001*, equity granted under Cochlear equity incentive schemes must remain at risk until vested, or until exercised if options. It is a specific condition of grant that no schemes are entered into, by an individual or their associates, that specifically protect the unvested value of options or performance rights allocated.

Cochlear also prohibits executive KMP providing Cochlear securities in connection with a margin loan or similar financing arrangement unless that person has received a specific notice of no objection in compliance with the policy.

3.7.4 Cessation of employment provisions

On 26 May 2015, the Company announced that Chris Roberts would be stepping down as CEO/P on 31 August 2015. In keeping with the terms of Chris Roberts' executive service contract entered into on 1 February 2004, Chris Roberts received an end of service payment of \$1,410,801, plus \$137,617 in statutory entitlements. In line with IFRS, these were accrued at 30 June 2015 and were paid on 31 August 2015.

The Board used its discretion to permit Chris Roberts to retain 123,023 options from the 2013 CEIP and 2,781 performance rights from the 2013 CEIP (deferred STI) subject to existing performance hurdles and timeframes. Awards from the 2014 CEIP LTI grant were forfeited (see the table in section 4.2.3 for more details).

3.7.5 Service contracts

Cochlear does not enter into service contracts for executive KMP. The terms for executive KMP meet local employment law requirements. Key provisions are similar but do, on occasion, vary to suit different needs.

The following sets out details of the employment agreements relating to executive KMP:

Length of contract	Permanent contracts until notice is given by either party.
Notice periods	Executive KMP are required to give between 60 days' and six months' written notice. Cochlear is required to give between 60 days' and 12 months' written notice (exact period specified in each contract).
Resignation	On resignation, unless the Board determines otherwise, all unvested STI or LTI benefits are forfeited.
Redundancy	If Cochlear terminates employment for reasons of redundancy, under Cochlear policy a severance payment comprises up to 12 months' fixed pay. STI and LTI benefits may be allowed to remain subject to performance criteria and vesting date, on a pro-rata basis, at the discretion of the Board with regard to the circumstances.
Death or total and permanent disability	On death or total and permanent disability, the Board has discretion to allow all unvested STI and LTI benefits to vest, in full or on a pro-rata basis.
Termination for serious misconduct	Cochlear may immediately terminate employment at any time in the case of serious misconduct, and executive KMP will only be entitled to payment of fixed pay up to the date of termination. On termination without notice by Cochlear in the event of serious misconduct: <ul style="list-style-type: none"> • all unvested STI or LTI benefits will be forfeited; and • any equity instruments provided to the employee on vesting of STI or LTI awards that are held in trust, or subject to a holding lock, will be forfeited. At the Board's discretion, Cochlear may seek reimbursement of amounts previously paid (see section 3.7.2 (Clawback)).
Statutory entitlements	Payment of statutory entitlements of long service leave and annual leave applies in all events of separation.
Other arrangements	Richard Brook - President, European, Middle East and African Regions will receive: <ul style="list-style-type: none"> • a maximum of CHF 30,000 for repatriation costs in the case of termination or resignation.
Post-employment restraints	All executive KMP are subject to post-employment restraints for up to 12 months.

4. Employee share scheme and other share information

This section provides:

1. a description of the employee share schemes (ESS) Cochlear uses to provide equity rewards to Cochlear employees;
2. disclosures required in relation to ESS grants provided to executive KMP;
3. disclosures required in relation to ESS instruments that Cochlear has issued; and
4. disclosures required in relation to Cochlear Limited shares and other ESS instruments held by executive KMP.

4.1 Employee share schemes operated by Cochlear

Plan details	Type of instruments	Details	Purpose
<p>Cochlear Employee Share Plan (CESP)</p> <p>Date established: 1999</p>	<p>Ordinary shares held under holding lock</p>	<p>Issue of ordinary shares annually to eligible employees.</p>	<p>The purpose of the CESP is to encourage general employee equity participation through tax concessional legislation which currently facilitates tax effective issues of up to \$1,000 of shares annually per eligible employee. Under the September 2015 (FY16) grant, 1,343 employees in Australia and Belgium each received an award of 12 shares. Executive KMP are not eligible for this program.</p>
<p>APAC Employee Equity Plan (AEEP)</p> <p>Date established: 2016</p>	<p>Service rights held under holding lock</p>	<p>Issue of service rights annually to eligible employees within the Asia Pacific region.</p>	<p>The AEEP replaces the Cash Incentive Plan that was previously in place for selected Asian countries and aligns with the CESP via provision of up to \$1,000 of service rights annually per eligible employee. Upon vesting, each service right converts to one share. Under the FY16 grant, 112 employees each received an award of 13 service rights. Executive KMP are not eligible for this program.</p>
<p>Cochlear Executive Incentive Plan (CEIP)</p> <p>Date established: 2013</p>	<p>Performance rights and options</p>	<p>A performance incentive scheme designed to reward participants for achieving market competitive business outcomes. Participants receive an award based on a predetermined formula, as approved by the Board from time to time based on market standards and trends.</p>	<p>The purpose of the CEIP is to encourage employees and executives to hold Cochlear shares, and to align their interests to shareholders' interests. Under the LTI, vesting of options or performance rights occurs only if Cochlear achieves challenging and market competitive EPS growth and relative TSR hurdles. The first grant of options and performance rights under the CEIP was made on 15 October 2013. Also refer to section 3.6.2. Under the deferred STI, grants are based on performance in the prior year, and provide more certainty of building an equity holding as no further performance hurdles apply other than tenure.</p>

4.2 Employee share scheme grants to executive KMP

4.2.1 Analysis of share based payments granted as remuneration

The vesting profile of the options and performance shares/rights granted as remuneration to each executive KMP is set out below:

Name	Reward vehicle	Grant date	Vesting date	Options			Performance shares/rights ¹		
				Number granted	Number vested	Number forfeited/lapsed	Number granted	Number vested	Number forfeited/lapsed
Chris Roberts	FY13 CELTIP	13-Aug-12	17-Aug-15	231,161	115,580	115,581	-	-	-
	FY14 CEIP LTI	15-Oct-13	15-Aug-16	123,023	-	-	-	-	-
	FY14 CEIP deferred STI	12-Aug-14	12-Aug-16	-	-	-	2,781	-	-
	FY15 CEIP LTI	14-Oct-14	12-Aug-17	60,771	-	60,771	11,821	-	11,821
	FY15 CEIP deferred STI	18-Aug-15	18-Aug-17	-	-	-	5,063	-	-
	FY16 CEIP LTI	2-Nov-15	17-Aug-18	-	-	-	-	-	-
	Total			414,955	115,580	176,352	19,665	-	11,821
Chris Smith	FY13 CELTIP	13-Aug-12	17-Aug-15	45,063	22,531	22,532	1,577	788	789
	FY14 CEIP LTI	15-Oct-13	15-Aug-16	14,955	-	-	3,198	-	-
	FY14 CEIP deferred STI	12-Aug-14	12-Aug-16	-	-	-	1,199	-	-
	FY15 CEIP LTI	14-Oct-14	12-Aug-17	15,412	-	-	2,998	-	-
	FY15 CEIP deferred STI	18-Aug-15	18-Aug-17	-	-	-	2,027	-	-
	FY16 CEIP LTI	2-Nov-15	17-Aug-18	69,047	-	-	5,641	-	-
	Total			144,477	22,531	22,532	16,640	788	789
Richard Brook	FY13 CELTIP	13-Aug-12	17-Aug-15	41,448	20,724	20,724	-	-	-
	FY14 CEIP LTI	15-Oct-13	15-Aug-16	7,249	-	-	3,617	-	-
	FY14 CEIP deferred STI	12-Aug-14	12-Aug-16	-	-	-	993	-	-
	FY15 CEIP LTI	14-Oct-14	12-Aug-17	7,256	-	-	3,293	-	-
	FY15 CEIP deferred STI	18-Aug-15	18-Aug-17	-	-	-	1,448	-	-
	FY16 CEIP LTI	2-Nov-15	17-Aug-18	12,601	-	-	2,402	-	-
	Total			68,554	20,724	20,724	11,753	-	-
Dig Howitt	FY13 CELTIP	13-Aug-12	17-Aug-15	-	-	-	6,095	3,047	3,048
	FY14 CEIP LTI	15-Oct-13	15-Aug-16	21,900	-	-	-	-	-
	FY14 CEIP deferred STI	12-Aug-14	12-Aug-16	-	-	-	714	-	-
	FY15 CEIP LTI	14-Oct-14	12-Aug-17	10,970	-	-	2,133	-	-
	FY15 CEIP deferred STI	18-Aug-15	18-Aug-17	-	-	-	1,066	-	-
	FY16 CEIP LTI	2-Nov-15	17-Aug-18	18,682	-	-	-	-	-
	Total			51,552	-	-	10,008	3,047	3,048
Jan Janssen	FY13 CELTIP	13-Aug-12	17-Aug-15	26,491	13,245	13,246	2,473	1,236	1,237
	FY14 CEIP LTI	15-Oct-13	15-Aug-16	6,664	-	-	3,325	-	-
	FY14 CEIP deferred STI	12-Aug-14	12-Aug-16	-	-	-	725	-	-
	FY15 CEIP LTI	14-Oct-14	12-Aug-17	11,127	-	-	2,164	-	-
	FY15 CEIP deferred STI	18-Aug-15	18-Aug-17	-	-	-	1,177	-	-
	FY16 CEIP LTI	2-Nov-15	17-Aug-18	9,736	-	-	1,856	-	-
	Total			54,018	13,245	13,246	11,720	1,236	1,237
Tony Manna	FY13 CELTIP	13-Aug-12	17-Aug-15	18,124	9,062	9,062	-	-	-
	FY14 CEIP LTI	15-Oct-13	15-Aug-16	-	-	-	-	-	-
	FY14 CEIP deferred STI	12-Aug-14	12-Aug-16	-	-	-	1,359	-	-
	FY15 CEIP LTI	14-Oct-14	12-Aug-17	-	-	-	-	-	-
	FY15 CEIP deferred STI	18-Aug-15	18-Aug-17	-	-	-	1,542	-	-
	FY16 CEIP LTI	2-Nov-15	17-Aug-18	10,216	-	-	834	-	-
	Total			28,340	9,062	9,062	3,735	-	-
Neville Mitchell	FY13 CELTIP	13-Aug-12	17-Aug-15	10,928	5,464	5,464	6,120	3,060	3,060
	FY14 CEIP LTI	15-Oct-13	15-Aug-16	13,723	-	-	2,934	-	-
	FY14 CEIP deferred STI	12-Aug-14	12-Aug-16	-	-	-	893	-	-
	FY15 CEIP LTI	14-Oct-14	12-Aug-17	8,168	-	-	3,707	-	-
	FY15 CEIP deferred STI	18-Aug-15	18-Aug-17	-	-	-	1,444	-	-
	FY16 CEIP LTI	2-Nov-15	17-Aug-18	7,159	-	-	3,184	-	-
	Total			39,978	5,464	5,464	18,282	3,060	3,060

1. For grants made under the CELTIP for 2012, participants were granted either options or performance shares, so all holdings referred to under the "Performance shares/rights" columns granted for 2012 represent performance shares. Under the CEIP, participants were granted either options or performance rights, so all holdings referred to under "Performance shares/rights" columns granted from 2013 onwards represent performance rights.

The options granted in FY16 have an exercise price of \$82.89 and an expiration date of 16 March 2019. Fair values of FY16 option and performance rights granted under the LTI plan are as follows:

Fair value (IFRS-2)	Options	Performance rights
EPS based	\$14.70	\$77.11
TSR based	\$12.41	\$54.43

4.2.2 Exercise of options and performance shares/rights granted as remuneration

During FY16, 182,044 options were exercised by executive KMP. The FY13 CEIP grant met the EPS hurdle so there was a 50% vesting from this grant.

There are no amounts unpaid on the shares issued as a result of the exercise of the options in prior years.

4.2.3 Analysis of movement in options and shares

The tables below detail movements in number and value during FY16 of:

- options over ordinary shares of Cochlear Limited acquired under the CELTIP and CEIP LTI; and
- performance shares/rights acquired under the CELTIP, CEIP LTI and CEIP deferred STI, held by executive KMP.

Options	Opening		Granted in year		Exercised in year		Forfeited/ lapsed in year	Closing
	Number		Number	Value (\$) ¹	Number	Intrinsic value (\$) ²	Number	Number
Chris Roberts ³	414,955		-	-	115,580	2,583,213	176,352	N/A
Chris Smith	75,430		69,047	935,771	22,531	490,489	22,532	99,414
Richard Brook	55,953		12,601	170,777	20,724	469,399	20,724	27,106
Dig Howitt	32,870		18,682	253,191	-	-	-	51,552
Jan Janssen	44,282		9,736	131,949	13,245	302,913	13,246	27,527
Tony Manna	18,124		10,216	138,454	4,500	185,085	9,062	14,778
Neville Mitchell	32,819		7,159	97,024	5,464	124,962	5,464	29,050
Total	674,433		127,441	1,727,166	182,044	4,156,061	247,380	249,427

Performance shares/rights	Opening		Granted in year			Exercised in year		Forfeited/ lapsed in year	Closing
	Number	LTI number	LTI value (\$) ¹	Deferred STI number	Deferred STI value (\$) ⁴	Number	Intrinsic value (\$) ⁵	Number	Number
Chris Roberts ^{3,6}	14,602	-	-	5,063	401,496	-	-	11,821	N/A
Chris Smith	8,972	5,641	371,014	2,027	160,741	788	66,980	789	15,063
Richard Brook	7,903	2,402	157,982	1,448	114,826	-	-	-	11,753
Dig Howitt	8,942	-	-	1,066	84,534	3,047	260,427	3,048	3,913
Jan Janssen	8,687	1,856	122,071	1,177	93,336	1,236	105,863	1,237	9,247
Tony Manna	1,359	834	54,853	1,542	122,281	-	-	-	3,735
Neville Mitchell	13,654	3,184	209,415	1,444	114,509	3,060	262,089	3,060	12,162
Total	64,119	13,917	915,335	13,767	1,091,723	8,131	695,359	19,955	55,873

1. The value derived under IFRS-2 of options and performance rights granted during the financial year is the value of the options and performance rights calculated at grant date using the Black-Scholes-Merton pricing model discounted for vesting probabilities of performance criteria. The total value of the options and performance rights granted is included in the table above. This amount is allocated to remuneration over the vesting period (i.e. in each of FY16 to FY18).

2. The intrinsic value of exercised options is calculated as the closing market price of Cochlear shares on the ASX on the date of exercise less the applicable exercise price times the number of options.

3. For Chris Roberts closing balances at 30 June 2016 have not been disclosed as he retired on 31 August 2015.

4. Deferred STI value represents performance rights under the CEIP deferred STI plan.

5. The intrinsic value of vested performance shares calculated as at the closing market price of shares of the Company on the ASX on the date of vesting times the number of performance shares.

6. The "Granted in year" deferred STI performance rights were forfeited at the discretion of the Board at the end of Chris Roberts' service on 31 August 2015.

4.3 Potential dilution if options vest and ordinary shares issued - Unaudited

At the date of this report, the number of ordinary shares that would be issued if all options were vested, having met the service and performance conditions, and exercised and assuming ordinary shares were issued, is as follows:

Grant date	Number of options				Exercise price per share (\$)	Exercise period	Current net value of outstanding options as at 30 June 2016 (\$)¹
	Issued	Exercised	Forfeited/lapsed	At report date			
13-Aug-12	759,828	328,885	416,948	13,995	62.78	Aug-15 to 30-Jun-17	818,288
15-Oct-13²	224,314	-	10,239	214,075	59.13	Aug-16 to 10-Mar-17	13,298,339
14-Oct-14²	138,963	-	60,771	78,192	68.56	Aug-17 to 9-Mar-18	4,119,936
2-Nov-15²	162,451	-	12,460	149,991	82.89	Aug-18 to 16-Mar-19	5,753,655
Total	1,285,556	328,885	500,418	456,253			23,990,218

1. Share price as at 30 June 2016 was \$121.25.

2. Lapsed options from unvested grants relate to plan members who have departed Cochlear.

The total current net value of the options is equivalent to 197,857 shares. In addition, there are 140,058 unvested performance rights and 56,959 shares held under holding lock. The total potential dilution under employee equity plans is equivalent to 394,874 shares or 0.7% of issued capital.

4.4 KMP equity interests - Audited

In accordance with the *Corporations Act 2001* (section 205G(1)), Cochlear is required to notify the interests (shares and rights to shares) of directors to the ASX. In the interests of transparency and completeness of disclosure, this information is provided for each NED in section 2.3 (as required under the *Corporations Act 2001*) and all executive KMP as well. Please refer sections 3.7.1 and 3.7.3 (Minimum shareholding guidelines and Hedging and margin lending prohibition).

The table below indicates Cochlear Limited shareholding including any vested but unexercised options and performance shares:

Executive KMP	Held at 1 July 2015	Purchases	Received on exercise of options and performance shares	Sales	Cochlear Limited ordinary shares held as at 30 June 2016	Vested options over Cochlear Limited ordinary shares¹	Policy value of Cochlear Limited securities as at year end (\$)²
Executive director							
Chris Smith	-	-	23,319	5,031	18,288	-	1,770,827
Other executive KMP							
Richard Brook	7,700	-	20,724	20,424	8,000	-	774,640
Dig Howitt	21,351	-	3,047	3,000	21,398	-	2,071,968
Jan Janssen	5,898	-	14,481	5,000	15,379	-	1,489,149
Tony Manna	-	-	4,500	4,500	-	4,562	77,668
Neville Mitchell	11,000	-	8,524	8,524	11,000	-	1,065,130
Total executive KMP	45,949	-	74,595	46,479	74,065	4,562	7,249,382

1. The number of vested but unexercised options.

2. In line with the Share Ownership Policy (available on our website), the Policy value of Cochlear Limited ordinary shares is calculated using the average daily share price over the previous 12 months as at closing on the ASX up to 30 June 2016, times the number of shares. The Policy value of vested options is calculated using the average daily share price over the previous 12 months as at closing on the ASX up to 30 June 2016 less the applicable exercise price times the number of options (negative values are treated as zero in the totals). The Policy allows only half of the monetary gain of vested but unexercised options. Total Policy value of securities is therefore the sum of the value of shares plus half of the monetary gain of unexercised options.

All executive KMP are compliant with the minimum shareholding guidelines.

The table below indicates any unvested options and performance rights issued to executive KMP but still subject to performance hurdles and deferred STI service conditions:

	Unvested options over Cochlear Limited ordinary shares ¹	Unvested LTI performance rights over Cochlear Limited ordinary shares ²	Unvested deferred STI performance rights over Cochlear Limited ordinary shares ³	Total intrinsic value of unvested options and performance rights as at year end (\$) ⁴
Executive director				
Chris Smith	99,414	11,837	3,226	3,788,427
Other executive KMP				
Richard Brook	27,106	9,312	2,441	2,079,118
Dig Howitt	51,552	2,133	1,780	1,870,611
Jan Janssen	27,527	7,345	1,902	1,822,701
Tony Manna	14,778	834	2,901	595,288
Neville Mitchell	29,050	9,825	2,337	2,322,688
Total executive KMP	249,427	41,286	14,587	12,478,833

1. The number of unvested options.

2. The number of unvested CEIP LTI performance rights.

3. The number of unvested CEIP deferred STI performance rights.

4. The intrinsic value of unvested performance rights calculated as at the closing Cochlear Limited share price on the ASX on 30 June 2016 times the number of performance rights and the intrinsic value of unvested options calculated as at the closing Cochlear Limited share price on the ASX on 30 June 2016 less the applicable exercise price times the number of options (negative values are treated as zero in the totals).

All executive KMP are compliant with the Share Ownership Policy (minimum shareholding requirements).

Indemnification of officers

Under the terms of Article 35 of the Company's Constitution, and to the extent permitted by law, the Company has indemnified the directors of the Company named in this Directors' Report, the Company Secretary, Mr NJ Mitchell, and other persons concerned in or taking part in the management of the Consolidated Entity. The indemnity applies when persons are acting in their capacity as officers of the Company in respect of:

- liability to third parties (other than the Company or related bodies corporate), if the relevant officer has acted in good faith; and
- costs and expenses of successfully defending legal proceedings in which relief under the *Corporations Act 2001* is granted to the relevant officer.

Insurance premiums

During the financial year, the Company paid a premium for a Directors' and Officers' Liability Insurance policy. The insurance provides cover for the directors named in this Directors' Report, the Company Secretary, and officers and former directors and officers of the Company. The insurance also provides cover for present and former directors and officers of other companies in the Consolidated Entity. The directors have not included in this report details of the nature of the liabilities covered and the amount of the premium paid in respect of the Directors' and Officers' Liability and Supplementary Legal Expenses Insurance policies, as such disclosure is prohibited under the terms of the contract.

Events subsequent to the reporting date

Other than the matter noted below, there has not arisen in the interval between the end of the financial year and the date of this Directors' Report, any item, transaction or event of a material and unusual nature likely, in the opinion of the directors of the Company, to affect significantly the operations of Cochlear, the results of those operations, or the state of affairs of Cochlear in future financial years:

Dividends

For dividends declared after 30 June 2016, see Note 2.6 to the financial statements.

Lead auditor's independence declaration

The lead auditor's independence declaration is set out on page 51 and forms part of the Directors' Report for the financial year ended 30 June 2016.

Rounding off

The Company is of a kind referred to in Australian Securities and Investments Commission (ASIC) (Rounding in Financial/Directors' Reports) Instrument 2016/191 (Rounding instrument) dated 24 March 2016 and in accordance with that Instrument, amounts in the Directors' Report and Financial Report have been rounded off to the nearest one thousand dollars unless otherwise indicated.

Dated at Sydney this 9th day of August 2016.

Signed in accordance with a resolution of the directors:



Director



Director



Lead auditor's independence declaration under section 307C of the *Corporations Act 2001*

To: the directors of Cochlear Limited

I declare that, to the best of my knowledge and belief, in relation to the audit for the year ended 30 June 2016 there have been:

- (i) no contraventions of the auditor independence requirements as set out in the *Corporations Act 2001* in relation to the audit; and
- (ii) no contraventions of any applicable code of professional conduct in relation to the audit.

KPMG

Sydney, 9 August 2016

Cameron Slapp, Partner

INCOME STATEMENT Cochlear Limited and its controlled entities for the year ended 30 June 2016

	Note	2016 \$000	2015 \$000
Revenue	2.2	1,130,552	925,630
Cost of sales	2.3(a)	(333,593)	(275,320)
Gross profit		796,959	650,310
Selling and general expenses		(326,090)	(260,809)
Administration expenses		(79,287)	(59,536)
Research and development expenses		(143,134)	(127,985)
Other income	2.4	14,156	4,428
Results from operating activities		262,604	206,408
Finance income - interest		468	300
Finance expense - interest		(8,806)	(10,405)
Net finance expense		(8,338)	(10,105)
Profit before income tax		254,266	196,303
Income tax expense	3.1	(65,345)	(50,463)
Net profit		188,921	145,840
Basic earnings per share (cents)	2.5	330.6	256.1
Diluted earnings per share (cents)	2.5	330.0	254.8

The notes on pages 57 to 83 are an integral part of these consolidated financial statements.

STATEMENT OF COMPREHENSIVE INCOME Cochlear Limited and its controlled entities for the year ended 30 June 2016

	2016	2015
	\$000	\$000
Net profit	188,921	145,840
<i>Other comprehensive (loss)/income</i>		
Items that will not be reclassified subsequently to the income statement:		
Defined benefit plan actuarial losses	(2,000)	(1,806)
Total items that will not be reclassified subsequently to the income statement	(2,000)	(1,806)
Items that may be reclassified subsequently to the income statement:		
Foreign currency translation differences	(15,832)	20,089
Effective portion of changes in fair value of cash flow hedges, net of tax	5,431	(32,412)
Net change in fair value of cash flow hedges transferred to the income statement, net of tax	19,305	11,389
Total items that may be reclassified subsequently to the income statement	8,904	(934)
Other comprehensive income/(loss), net of tax	6,904	(2,740)
Total comprehensive income	195,825	143,100

The notes on pages 57 to 83 are an integral part of these consolidated financial statements.

	Note	2016 \$000	2015 \$000
Assets			
Cash and cash equivalents	2.7(a)	75,417	72,208
Trade and other receivables	6.4(b)	281,925	249,744
Forward exchange contracts		11,454	3,853
Inventories	5.1	154,103	145,861
Current tax assets	3.2	6,208	3,606
Prepayments		13,921	13,754
Total current assets		543,028	489,026
Other receivables		1,507	63
Forward exchange contracts		10,713	1,910
Property, plant and equipment	5.2	86,878	80,809
Intangible assets	5.3	224,338	228,531
Investments	5.4	13,755	-
Deferred tax assets	3.2	77,144	75,063
Total non-current assets		414,335	386,376
Total assets		957,363	875,402
Liabilities			
Trade and other payables		110,354	99,858
Forward exchange contracts		12,643	24,162
Loans and borrowings	6.3	3,978	168,159
Current tax liabilities	3.2	13,701	20,645
Employee benefit liabilities	4.2	45,485	43,223
Provisions	5.5	33,675	26,652
Deferred revenue		31,264	20,585
Total current liabilities		251,100	403,284
Forward exchange contracts		3,547	10,961
Loans and borrowings	6.3	189,260	44,552
Employee benefit liabilities	4.2	13,750	11,479
Provisions	5.5	44,027	43,394
Deferred tax liabilities	3.2	7,122	6,346
Total non-current liabilities		257,706	116,732
Total liabilities		508,806	520,016
Net assets		448,557	355,386
Equity			
Share capital		158,940	144,136
Reserves		(14,662)	(26,201)
Retained earnings		304,279	237,451
Total equity		448,557	355,386

The notes on pages 57 to 83 are an integral part of these consolidated financial statements.

STATEMENT OF CHANGES IN EQUITY Cochlear Limited and its controlled entities for the year ended 30 June 2016

Amounts \$000	Issued capital	Treasury reserve	Translation reserve	Hedging reserve	Share based payment reserve	Retained earnings	Total equity
2015							
Balance at 1 July 2014	152,599	(8,463)	(52,630)	476	19,963	217,260	329,205
<i>Total comprehensive income/(loss)</i>							
Net profit	-	-	-	-	-	145,840	145,840
<i>Other comprehensive (loss)/income</i>							
Defined benefit plan actuarial losses	-	-	-	-	-	(1,806)	(1,806)
Foreign currency translation differences	-	-	20,089	-	-	-	20,089
Effective portion of changes in fair value of cash flow hedges, net of tax	-	-	-	(32,412)	-	-	(32,412)
Net change in fair value of cash flow hedges transferred to the income statement, net of tax	-	-	-	11,389	-	-	11,389
Total other comprehensive income/(loss)	-	-	20,089	(21,023)	-	(1,806)	(2,740)
Total comprehensive income/(loss)	-	-	20,089	(21,023)	-	144,034	143,100
Transactions with owners, recorded directly in equity							
Share based payment transactions	-	-	-	-	6,004	-	6,004
Deferred tax recognised in equity	-	-	-	-	920	-	920
Dividends to shareholders	-	-	-	-	-	(123,843)	(123,843)
Balance at 30 June 2015	152,599	(8,463)	(32,541)	(20,547)	26,887	237,451	355,386
2016							
Balance at 1 July 2015	152,599	(8,463)	(32,541)	(20,547)	26,887	237,451	355,386
<i>Total comprehensive income/(loss)</i>							
Net profit	-	-	-	-	-	188,921	188,921
<i>Other comprehensive (loss)/income</i>							
Defined benefit plan actuarial losses	-	-	-	-	-	(2,000)	(2,000)
Foreign currency translation differences	-	-	(15,832)	-	-	-	(15,832)
Effective portion of changes in fair value of cash flow hedges, net of tax	-	-	-	5,431	-	-	5,431
Net change in fair value of cash flow hedges transferred to the income statement, net of tax	-	-	-	19,305	-	-	19,305
Total other comprehensive (loss)/income	-	-	(15,832)	24,736	-	(2,000)	6,904
Total comprehensive (loss)/income	-	-	(15,832)	24,736	-	186,921	195,825
Transactions with owners, recorded directly in equity							
Performance shares vested	-	2,099	-	-	(2,099)	-	-
Share options exercised	6,704	6,001	-	-	(3,502)	-	9,203
Share based payment transactions	-	-	-	-	8,342	-	8,342
Deferred tax recognised in equity	-	-	-	-	(106)	-	(106)
Dividends to shareholders	-	-	-	-	-	(120,093)	(120,093)
Balance at 30 June 2016	159,303	(363)	(48,373)	4,189	29,522	304,279	448,557

The notes on pages 57 to 83 are an integral part of these consolidated financial statements.

STATEMENT OF CASH FLOWS Cochlear Limited and its controlled entities for the year ended 30 June 2016

	Note	2016 \$000	2015 \$000
<i>Cash flows from operating activities</i>			
Cash receipts from customers		1,105,512	919,280
Cash paid to suppliers and employees		(834,884)	(694,288)
Grant and other income received		5,461	3,250
Interest received		454	297
Interest paid		(10,745)	(7,627)
Income taxes paid		(80,685)	(32,211)
Net cash provided by operating activities	2.7(b)	185,113	188,701
<i>Cash flows from investing activities</i>			
Acquisition of property, plant and equipment		(28,858)	(23,897)
Proceeds from sale of non-current assets		1,175	-
Acquisition of enterprise resource planning system		(7,556)	(4,530)
Acquisition of other intangible assets		(1,140)	-
Acquisition of investments	5.4	(13,755)	-
Net cash used in investing activities		(50,134)	(28,427)
<i>Cash flows from financing activities</i>			
Repayments of borrowings		(332,971)	(148,701)
Proceeds from borrowings		312,971	123,701
Net proceeds from exercise of share options		9,203	-
Dividends paid	2.6	(120,093)	(123,843)
Net cash used in financing activities		(130,890)	(148,843)
Net increase in cash and cash equivalents		4,089	11,431
Cash and cash equivalents, net of overdrafts at 1 July		72,208	56,127
Effect of exchange rate fluctuations on cash held		(880)	4,650
Cash and cash equivalents, net of overdrafts at 30 June	2.7(a)	75,417	72,208

The notes on pages 57 to 83 are an integral part of these consolidated financial statements.

1. Basis of preparation

This section sets out the Company's accounting policies that relate to the financial statements as a whole. Where an accounting policy is specific to one note, the policy is described in the note to which it relates.

1.1 Reporting entity

Cochlear Limited (the Company) is a company domiciled in Australia. The consolidated financial statements of the Company as at and for the year ended 30 June 2016 comprise the Company and its controlled entities (together referred to as Cochlear or the Consolidated Entity). Cochlear is a for-profit entity and operates in the implantable hearing device industry.

1.2 Basis of preparation

(a) Statement of compliance

The Financial Report is a general purpose financial report which has been prepared in accordance with Australian Accounting Standards (AASBs) adopted by the Australian Accounting Standards Board and the *Corporations Act 2001*. The consolidated financial statements comply with International Financial Reporting Standards (IFRS) and Interpretations adopted by the International Accounting Standards Board.

The Board of directors approved the consolidated financial statements on 9 August 2016.

(b) Basis of measurement

The consolidated financial statements have been prepared on the historical cost basis except for derivative financial instruments which are measured at fair value. The fair value measurement method of derivative instruments is discussed further in Note 6.4(d).

(c) Functional and presentation currency

These consolidated financial statements are presented in Australian dollars (AUD), which is the Company's functional currency.

The Company is of a kind referred to in ASIC Corporations (Rounding in Financial/Directors' Reports) Instrument 2016/191 (Rounding instrument) dated 24 March 2016 and in accordance with that Instrument, all financial information presented in AUD has been rounded to the nearest one thousand dollars unless otherwise stated.

(d) Foreign currency

Foreign currency transactions

Transactions in foreign currencies are translated to the respective functional currencies of entities at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated to the functional currency at the foreign exchange rate ruling at that date. Non-monetary assets and liabilities denominated in foreign currencies that are stated at historical cost are translated using the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated to the functional currency at the foreign exchange rates ruling at the date the fair value was determined.

Foreign exchange differences arising on translation are recognised in the income statement.

Financial statements of foreign operations

The assets and liabilities of foreign operations are translated to the Company's functional currency at foreign exchange rates ruling at the reporting date.

The revenues and expenses of foreign operations are translated to the Company's functional currency at rates approximating the foreign exchange rates ruling at the dates of transactions.

Foreign currency differences arising from translation of controlled entities are recognised in the foreign currency translation reserve (translation reserve) in equity. When a foreign operation is disposed of, in part or in full, the relevant amount of its translation reserve is transferred to the income statement and reported as part of the gain or loss on disposal.

Foreign exchange gains and losses arising from a monetary item receivable from or payable to a foreign operation, the settlement of which is neither planned nor likely in the foreseeable future, are considered to form part of a net investment in a foreign operation and are recognised in other comprehensive income, and presented in the translation reserve.

(e) Use of judgements and estimates

The preparation of financial statements in conformity with IFRS requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the financial year in which the estimate is revised and in any future years affected.

Management discussed with the Audit Committee the development, selection and disclosure of Cochlear's critical accounting policies and estimates and the application of these policies and estimates.

Information about critical judgements in applying accounting policies that have the most significant effect on the amounts recognised in the consolidated financial statements is included in the following notes:

Note 4.2 – Employee benefit liabilities

Note 4.3 – Share based payments

Note 5.3 – Intangible assets

Note 5.5 – Provisions

Note 5.6 – Contingent liabilities

Note 6.4 – Financial risk management.

(f) Basis of consolidation

Controlled entities

The Consolidated Entity controls an entity when it is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The financial statements of controlled entities are included in the consolidated financial statements from the date that control commences until the date that control ceases.

Transactions eliminated on consolidation

Intra-group balances and transactions, and any unrealised income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements.

Special purpose entities

Cochlear has established special purpose entities (SPEs) for investment purposes. A SPE is consolidated if Cochlear concludes that it controls the SPE. SPEs controlled by Cochlear were established under terms that impose strict limitations on decision-making powers of the SPE's management.

(g) Goods and services tax (GST)

Revenues, expenses and assets are recognised net of the amount of GST. Where the amount of GST incurred is not recoverable from the taxation authority, the GST is recognised as part of the cost of acquisition of the asset or as part of the expense.

Receivables and payables are stated with the amount of GST included. The net amount of GST recoverable from, or payable to, the relevant taxation authority is included as a current asset or liability in the balance sheet.

Cash flows are included in the statement of cash flows on a gross basis. The GST components of cash flows arising from investing and financing activities which are recoverable from, or payable to, the relevant taxation authority are classified as operating cash flows.

2. Performance for the year

2.1 Operating segments

Cochlear's three reportable segments, determined on a geographical basis, are the strategic business units of Cochlear. Segment results, assets and liabilities include items directly attributable to a segment, as well as those that can be allocated on a reasonable basis. Unallocated items comprise corporate and other net expenses and corporate and manufacturing assets and liabilities.

Performance is measured based on segment earnings before interest and income tax (EBIT) as included in the internal management reports that are reviewed by Cochlear's Chief Executive Officer & President, who is also the chief operating decision-maker.

Information about reportable segments

	Americas		EMEA ¹		Asia Pacific		Total	
	2016	2015	2016	2015	2016	2015	2016	2015
	\$000	\$000	\$000	\$000	\$000	\$000	\$000	\$000
Reportable segment revenue	519,688	402,962	427,896	377,633	210,547	161,305	1,158,131	941,900
Reportable segment EBIT	276,931	204,879	180,925	172,113	64,842	47,292	522,698	424,284
Reportable segment assets	184,881	149,767	213,843	225,300	124,775	89,096	523,499	464,163
Reportable segment liabilities	49,257	41,524	47,132	42,721	32,772	18,719	129,161	102,964
Other material items								
Depreciation and amortisation	1,016	865	2,179	2,097	1,046	1,180	4,241	4,142
Write-down in value of inventories	302	14	250	534	175	308	727	856
Acquisition of non-current assets	741	351	1,769	1,842	973	347	3,483	2,540

1. Europe, Middle East and Africa.

Reconciliations of reportable segment revenues, profit or loss, assets and liabilities and other material items

Revenues	Cochlear implants	Services	Total Cochlear implants	Acoustics	Reportable segment revenue	Foreign exchange losses on hedged sales	Consolidated revenue
	\$000	\$000	\$000	\$000	\$000	\$000	\$000
2016	729,171	289,418	1,018,589	139,542	1,158,131	(27,579)	1,130,552
2015	604,346	222,458	826,804	115,096	941,900	(16,270)	925,630

Profit or loss	Reportable segment EBIT	Corporate and other net expenses	Foreign exchange losses on hedged sales	Net finance expense	Consolidated profit before income tax
	\$000	\$000	\$000	\$000	\$000
2016	522,698	(232,515)	(27,579)	(8,338)	254,266
2015	424,284	(201,606)	(16,270)	(10,105)	196,303

Assets and liabilities	Reportable segment assets	Corporate and manufacturing assets	Consolidated total assets	Reportable segment liabilities	Corporate and manufacturing liabilities	Consolidated total liabilities
	\$000	\$000	\$000	\$000	\$000	\$000
2016	523,499	433,864	957,363	129,161	379,645	508,806
2015	464,163	411,239	875,402	102,964	417,052	520,016

Other material items	Reportable segment total		Corporate and manufacturing total		Consolidated total	
	2016	2015	2016	2015	2016	2015
	\$000	\$000	\$000	\$000	\$000	\$000
Depreciation and amortisation	4,241	4,142	29,250	26,110	33,491	30,252
Write-down in value of inventories	727	856	15,566	9,269	16,293	10,125
Acquisition of non-current assets	3,483	2,540	47,826	25,887	51,309	28,427

2.2 Revenue

Sales revenue is revenue earned from the provision of products or services, net of returns, discounts and allowances.

Revenue from the sale of goods is recognised when the significant risks and rewards of ownership have been transferred to the buyer, recovery of the consideration is probable, the associated costs and possible return of goods can be estimated reliably, there is no continuing management involvement with the goods and the amount of revenue can be measured reliably.

Revenue from the sale of services is recognised when the service has been provided to the customer and where there are no continuing unfulfilled service obligations.

The accounting policy for foreign exchange gains/losses arising from hedges of forecast sales transactions is set out in Note 6.4(a).

	2016	2015
	\$000	\$000
Sale of goods before hedging	1,145,492	931,390
Foreign exchange losses on hedged sales	(27,579)	(16,270)
Revenue from sale of goods	1,117,913	915,120
Rendering of services	12,639	10,510
Total revenue	1,130,552	925,630

2.3 Expenses

	2016	2015
	\$000	\$000
(a) Cost of sales		
Carrying amount of inventories recognised as an expense	308,990	256,593
Other	8,310	8,602
Write-down in value of inventories	16,293	10,125
Total cost of sales	333,593	275,320
(b) Profit before income tax has been arrived at after charging the following item:		
Operating lease rental expense	26,261	24,420

2.4 Other income

Other income, including government grants, is recognised on a systematic basis over the years necessary to match it with the related costs for which it is intended to compensate. If the costs have already been incurred, the amount is recognised in the year the entitlement is confirmed. Foreign exchange gains are recognised in accordance with the accounting policy at Note 1.2(d).

	2016	2015
	\$000	\$000
Grant received or due and receivable	2,579	1,809
Net foreign exchange gain	8,695	1,178
Other income	2,882	1,441
Total other income	14,156	4,428

2.5 Earnings per share

Cochlear presents basic and diluted earnings per share (EPS) for its ordinary shares.

Basic earnings per share

The calculation of basic EPS has been based on the following net profit attributable to equity holders of the parent entity and weighted average number of ordinary shares of the Company:

	2016	2015
Net profit attributable to equity holders of the parent entity	\$188,921,000	\$145,840,000
<i>Weighted average number of ordinary shares (basic):</i>		
Issued ordinary shares at 1 July (number)	56,957,274	56,937,519
Effect of options and performance shares exercised (number)	175,635	-
Effect of shares issued under Employee Share Plan (number)	11,669	13,693
Weighted average number of ordinary shares (basic) at 30 June	57,144,578	56,951,212
Basic earnings per share (cents)	330.6	256.1

Diluted earnings per share

The calculation of diluted EPS has been based on the following net profit attributable to equity holders of the parent entity and weighted average number of shares outstanding after adjustments for the effects of all dilutive potential ordinary shares:

	2016	2015
Net profit attributable to equity holders of the parent entity	\$188,921,000	\$145,840,000
<i>Weighted average number of ordinary shares (diluted):</i>		
Weighted average number of shares (basic) (number)	57,144,578	56,951,212
Effect of options and performance shares and rights unvested (number)	98,707	277,028
Weighted average number of ordinary shares (diluted) at 30 June	57,243,285	57,228,240
Diluted earnings per share (cents)	330.0	254.8

2.6 Dividends

A liability for dividends payable is recognised in the financial year in which the dividends are declared.

	Dollars per share	Total amount \$000	Franked/unfranked	Date of payment
Dividends recognised in the current financial year by the Company are:				
2016				
Interim 2016 ordinary	1.10	62,925	100% Franked	1 April 2016
Final 2015 ordinary	1.00	57,168	100% Franked	1 October 2015
Total amount	2.10	120,093		
2015				
Interim 2015 ordinary	0.90	51,374	35% Franked	26 March 2015
Final 2014 ordinary	1.27	72,469	20% Franked	25 September 2014
Total amount	2.17	123,843		

Subsequent event

Since the end of the financial year, the directors declared the following dividends:

Final 2016 ordinary	1.20	68,646	100% Franked	29 September 2016
Total amount	1.20	68,646		

The financial effect of the 2016 final dividend will be recognised in the subsequent financial year as it was declared after 30 June 2016.

Dividend franking account

Franked dividends paid during the financial year were franked at the tax rate of 30% (2015: 30%). There are no further tax consequences as a result of paying dividends other than a reduction in the franking account.

At 30 June 2016, there are \$25,101,000 of franking credits (2015: \$21,820,000) available to shareholders of Cochlear Limited for subsequent financial years.

The dividend franking account at year end is adjusted for:

- franking credits that will arise from the payment of the current tax liability;
- franking debits that will arise from the payment of dividends recognised as a liability at the year end; and
- franking credits that the Company may be prevented from distributing in subsequent financial years.

The ability to utilise the franking account credits is dependent upon the ability to declare dividends. The impact on the dividend franking account of dividends proposed after the balance sheet date but not recorded as a liability is to reduce it by \$29,409,152 (2015: \$24,463,618).

Dividends in excess of the dividend franking account balance will be unfranked.

2.7 Notes to the statement of cash flows

(a) Cash and cash equivalents

Cash and cash equivalents comprise cash balances and call deposits with an original maturity of three months or less. Bank overdrafts that are repayable on demand and form an integral part of Cochlear's cash management are included as a component of cash and cash equivalents for the purpose of the statement of cash flows.

Cash and cash equivalents at the reporting date as shown in the statement of cash flows are as follows:

	2016	2015
	\$000	\$000
Cash on hand	43,367	46,864
Cash on deposit	32,050	25,344
Cash and cash equivalents	75,417	72,208

(b) Reconciliation of net profit to net cash provided by operating activities

Net profit	188,921	145,840
Add items classified as investing activities:		
Loss on disposal of property, plant and equipment	335	617
Add non-cash items:		
Depreciation and amortisation	33,491	30,252
Equity settled share based payment transactions	8,342	6,004
Net cash provided by operating activities before changes in assets and liabilities	231,089	182,713
Changes in assets and liabilities:		
Change in trade and other receivables	(33,625)	(39,358)
Change in inventories	(8,242)	(17,248)
Change in prepayments	(167)	(1,168)
Change in deferred tax assets/liabilities	(11,186)	(5,536)
Change in trade and other payables	10,496	21,214
Change in current tax assets/liabilities	(9,546)	17,197
Change in employee benefit liabilities	4,533	14,885
Change in provisions	7,656	(1,049)
Change in deferred revenue	10,679	5,434
Effects of movements in foreign exchange	(16,574)	11,617
Net cash provided by operating activities	185,113	188,701

The operating cash account received an average interest rate of 0.47% (2015: 0.58%) per annum. Cash held on deposit for periods not exceeding 90 days received an average interest rate of 1.51% (2015: 1.70%) per annum.

3. Income taxes

The Company and its wholly owned Australian resident entities are part of a tax-consolidated group. As a consequence, all members of the tax-consolidated group are taxed as a single entity. The head entity within the tax-consolidated group is Cochlear Limited.

3.1 Income tax expense

Income tax expense includes current and deferred tax. Current and deferred tax are recognised in the income statement except to the extent that they relate to items recognised directly in other comprehensive income or equity.

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

Income tax expense recognised in the income statement

	Current year	Adjustment for prior years	Total current tax expense	Origination and reversal of temporary differences	Total deferred tax benefit	Total income tax expense
	\$000	\$000	\$000	\$000	\$000	\$000
2016	77,907	(1,270)	76,637	(11,292)	(11,292)	65,345
2015	54,051	1,028	55,079	(4,616)	(4,616)	50,463

Consolidated Entity - Numerical reconciliation between income tax expense and profit before income tax

	2016	2015
	\$000	\$000
Profit before income tax	254,266	196,303
Tax at the Australian tax rate of 30% (2015: 30%)	76,280	58,891
Increase in income tax expense due to:		
Non-deductible expenses	1,604	1,252
Effect of tax rate in foreign jurisdictions	6	-
Decrease in income tax expense due to:		
Research and development allowances	(11,275)	(9,029)
Effect of tax rate in foreign jurisdictions	-	(1,679)
	66,615	49,435
Adjustment for prior years	(1,270)	1,028
Income tax expense on profit before income tax	65,345	50,463

Tax expense relating to items relating to other comprehensive income/(loss) or equity

	Note	2016	2015
		\$000	\$000
Total deferred tax recognised in other comprehensive income/(loss) relating to derivative financial instruments	3.2	10,601	(9,010)
Total deferred tax recognised directly in equity relating to share based payments	3.2	106	(920)

Consolidated Entity - Numerical reconciliation between income tax expense and cash taxes paid

	2016	2015
	\$000	\$000
Income tax expense on profit before income tax	65,345	50,463
Timing differences recognised in deferred tax	6,333	(1,195)
Effect of tax rate in foreign jurisdictions	(66)	631
Current year tax instalments payable next year	(9,028)	(18,101)
Prior year tax instalments paid this year	18,101	413
Cash taxes paid per statement of cash flows	80,685	32,211

Cochlear Limited's Australian tax-consolidated group - Numerical reconciliation between income tax expense and profit before income tax

	2016	2015
	\$000	\$000
Profit before income tax (excluding dividends from wholly owned foreign subsidiaries)	200,913	154,528
Add: Dividends from wholly owned foreign subsidiaries	9,645	14,068
Profit before income tax	210,558	168,596
Tax at the Australian tax rate of 30% (2015: 30%)	63,167	50,579
Increase in income tax expense due to:		
Controlled foreign company income	2,337	851
Other non-deductible expenses	758	-
Decrease in income tax expense due to:		
Research and development allowances	(10,163)	(8,417)
Exempt foreign sourced dividends from wholly owned subsidiaries	(2,894)	(4,220)
Other non-assessable income	-	(1,037)
	53,205	37,756
Adjustment for prior years	203	(321)
Income tax expense on profit before income tax	53,408	37,435

3.2 Current and deferred tax assets and liabilities

Deferred tax is recognised on all temporary differences between the carrying amounts of assets and liabilities for financial reporting and taxation purposes.

The measurement of deferred tax mirrors the tax consequences that the Consolidated Entity expects to recover or settle the carrying amount of its assets and liabilities.

Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse.

A deferred tax asset is recognised to the extent that it is probable that future taxable profits will be available against which they can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced if it is no longer probable that the related tax benefit will be realised.

Recognised deferred tax assets and liabilities

	Assets		Liabilities		Net	
	2016	2015	2016	2015	2016	2015
	\$000	\$000	\$000	\$000	\$000	\$000
Property, plant and equipment	121	98	(2,500)	(1,523)	(2,379)	(1,425)
Intangible assets	63	57	(1,762)	(1,893)	(1,699)	(1,836)
Inventories	29,116	23,575	-	-	29,116	23,575
Provisions	33,932	30,338	-	-	33,932	30,338
Deferred revenue	1,488	1,380	-	-	1,488	1,380
Forward exchange contracts	-	8,808	(1,793)	-	(1,793)	8,808
Other	13,877	10,244	(2,860)	(2,930)	11,017	7,314
Tax losses carried forward	340	563	-	-	340	563
Deferred tax assets/(liabilities)	78,937	75,063	(8,915)	(6,346)	70,022	68,717
Set off of tax	(1,793)	-	1,793	-	-	-
Deferred tax assets/(liabilities)	77,144	75,063	(7,122)	(6,346)	70,022	68,717

Unrecognised deferred tax liabilities

At 30 June 2016, a deferred tax liability of \$11.0 million (2015: \$16.7 million) relating to investments in subsidiaries has not been recognised because the Company controls whether the asset will be recovered or the liability will be incurred and it is satisfied that it will not be incurred in the foreseeable future.

Movement in temporary differences during the year

	Note	2016 \$000	2015 \$000
Carrying amount at beginning of financial year		68,717	52,761
Recognised in the income statement	3.1	11,292	4,616
Recognised in other comprehensive income/(loss)	3.1	(10,601)	9,010
Recognised directly in equity	3.1	(106)	920
Effects of movements in foreign exchange		720	1,410
Carrying amount at end of financial year		70,022	68,717

Current tax assets and liabilities

The current tax assets for the Consolidated Entity of \$6.2 million (2015: \$3.6 million) represent the amount of income taxes recoverable in respect of current and prior years and arise from the payment of tax in excess of the amounts due to the relevant taxation authority. The current tax liabilities for the Consolidated Entity of \$13.7 million (2015: \$20.6 million) represent the amount of income taxes payable in respect of current and prior financial years.

4. Employee benefits

4.1 Employee expenses

	2016 \$000	2015 \$000
Wages and salaries	278,083	243,822
Contributions to superannuation plans	21,583	19,007
Increase in leave liabilities	2,925	2,806
Equity settled share based payment transactions	8,342	6,004
End of service payment	-	1,548
Total employee expenses	310,933	273,187

4.2 Employee benefit liabilities

Wages, salaries and annual leave

Liabilities for employee benefits for wages, salaries and annual leave are recognised in other payables and provisions if Cochlear has a present obligation to pay an amount as a result of past services provided by the employee. The liability is calculated on remuneration rates as at the reporting date including related on-costs, such as workers' compensation insurance and payroll tax.

Long service leave

The provision for long service leave is the present value of the estimated future cash outflows as a result of services provided by the employee up to the reporting date.

The provision is calculated using expected future increases in remuneration rates, including related on-costs, and expected settlement dates based on turnover history, and is discounted using the corporate bond rates which most closely match the terms to maturity of the related liabilities.

Defined benefit plans

The defined benefit obligations are calculated annually by a qualified actuary using the projected unit credit method. Remeasurements of the net defined benefit liability (excluding interest) are recognised immediately in other comprehensive income.

The Company determines the net interest expense (income) on the net defined benefit liability (asset) for the period by applying the discount rate used to measure the defined benefit obligation at the beginning of the period to the opening net defined benefit liability (asset), adjusted for any changes in the net defined benefit liability (asset) during the period resulting from contributions and benefit payments. Net interest expense related to defined benefit plans is recognised in the income statement.

These defined benefit plans cover, in aggregate, 91 employees. Cochlear contributed cash of \$1.5 million (2015: \$1.3 million) to defined benefit plans in the year ended 30 June 2016 and expects to contribute \$2.4 million in the year ending 30 June 2017.

Directors' retirement scheme

Non-executive directors appointed prior to 2003 were entitled to retirement benefits of up to three times their annual remuneration over the previous three years once they had more than five years' service. The ongoing accrual of benefits under the directors' retirement scheme ceased from 30 June 2007. The benefits accrued to that date are indexed by reference to the bank bill rate. As at 30 June 2016, Prof E Byrne, AC is the only non-executive director entitled to this benefit.

	2016	2015
	\$000	\$000
Current		
Provision for long service leave	8,478	7,370
Provision for annual leave	20,075	18,582
Provision for short-term incentives	16,932	15,723
Provision for end of service	-	1,548
Total current employee benefit liabilities	45,485	43,223
Non-current		
Provision for long service leave	5,429	5,105
Defined benefit plan	7,879	5,941
Provision for directors' retirement scheme	442	433
Total non-current employee benefit liabilities	13,750	11,479
Total employee benefit liabilities	59,235	54,702

4.3 Share based payments

From 1 July 2013, the Company grants options and performance rights to certain employees under the Cochlear Executive Incentive Plan (CEIP). Prior to July 2013, the Company granted options and performance shares to certain employees under the Cochlear Executive Long Term Incentive Plan (CELTIP).

The fair value of options, performance shares and performance rights granted is recognised as an employee expense, with a corresponding increase in equity. The expense is adjusted by the actual number of options, shares and rights that are expected to vest except where forfeiture is due to market related conditions.

The fair value is measured using the Black-Scholes-Merton pricing model at the date the options, performance shares or performance rights are granted, taking into account market based criteria and the terms and conditions attached to the instruments. The options, performance shares or performance rights are expensed over the vesting period after which the employees become unconditionally entitled to them.

When the Company grants options over its shares to employees of controlled entities, the fair value at grant date is recognised as an increase in the investment in subsidiaries, with a corresponding increase in equity over the vesting period of the grant in the Company's accounts.

The Company operates the Cochlear Executive Long Term Incentive Plan (Performance Shares) Trust (Trust). The main purpose of the Trust is to hold unvested performance shares as part of the CELTIP. Under IFRS, the Trust qualifies as an equity compensation plan special purpose entity and its results are included in those for the Company and the Consolidated Entity. Any shares held by the Trust are accounted for as treasury shares and treated as a reduction in the share capital of the Company and the Consolidated Entity.

At 30 June 2016, unissued ordinary shares of the Company under option and rights, and issued shares held in the Trust and the terms and conditions of the grants and issues are as follows:

Grant date	Exercise price of options	Number of options	Number of performance rights	Contractual life
August 2012 ¹	\$62.78	13,995	-	5 years
October 2013 ¹	\$59.13	214,075	16,419	4 years
August 2014 ²	N/A	-	32,836	2 years
October 2014 ¹	\$68.56	78,192	18,702	4 years
August 2015 ²	N/A	-	53,061	2 years
November 2015 ¹	\$82.89	149,991	17,584	4 years
Total		456,253	138,602	

1. Options and performance shares/rights offered under long-term incentives.

2. Performance rights offered under deferred short-term incentives.

Grants are split between short-term incentives (STI) and long-term incentives (LTI). For STI, certain employees under the CEIP are granted performance rights based on achievement of a mandatory portion of their STI. Grants are calculated at the end of each year and then held for two years until vesting.

Grants under LTI are in two equal tranches assigned to compound annual growth in EPS and ranking of TSR against the S&P/ASX 100. The conditions for minimum vesting are three years of service and:

- a minimum compound annual growth rate in EPS of 10% assigned to 50% of grant; or
- the Consolidated Entity's TSR is above the 50th percentile against the S&P/ASX 100 over three years assigned to 50% of grant.

The grant date fair value of options, performance rights and performance shares was measured based on the Black-Scholes-Merton pricing model. Expected volatility is estimated by considering historic average share price volatility. The inputs used in the measurement of the fair values at the grant date are the following:

	2 November 2015		18 August 2015	14 October 2014		12 August 2014
	EPS performance based conditions	TSR based conditions	STI deferral service based conditions	EPS performance based conditions	TSR based conditions	STI deferral service based conditions
Fair value of options at grant date	\$14.70	\$12.41	N/A	\$11.93	\$11.33	N/A
Fair value of performance rights at grant date	\$77.11	\$54.43	\$79.30	\$61.33	\$39.21	\$63.11
Share price at valuation date	\$85.13	\$85.13	\$85.13	\$67.85	\$67.85	\$67.85
Option exercise price	\$82.89	\$82.89	N/A	\$68.56	\$68.56	N/A
Expected volatility (weighted average volatility)	24.47%	24.47%	24.47%	29.49%	29.49%	29.49%
Option life	3 - 4 years	3 - 4 years	2 years	3 - 4 years	3 - 4 years	2 years
Expected dividend yield	3.41%	3.41%	3.41%	3.48%	3.48%	3.48%
Risk free interest rate (based on government bonds)	1.98%	1.98%	1.98%	2.54%	2.54%	2.54%

The number and weighted average exercise prices of options are as follows:

	Weighted average exercise price	Number of options	Weighted average exercise price	Number of options
	2016	2016	2015	2015
Outstanding at 1 July	\$62.80	1,038,834	\$64.18	1,416,328
Forfeited	\$64.23	(416,147)	\$68.13	(516,457)
Exercised	\$62.78	(328,885)	-	-
Granted	\$82.89	162,451	\$68.56	138,963
Outstanding at 30 June	\$68.67	456,253	\$62.80	1,038,834
Exercisable at 30 June	\$62.78	13,995	-	-

328,885 options were exercised in 2016. The weighted average market share price on the ASX at date of exercise was \$86.35 (2015: no options were exercised). The weighted average remaining contractual life of options outstanding at the end of the year is three years (2015: three years).

Employee Share Plan

Cochlear's Employee Share Plan (Plan) was approved by special resolution at the AGM held on 19 October 1999. Under the Plan, the directors can at their discretion, allocate at nil consideration up to a maximum of \$2,000 worth of shares per eligible employee in any one year. In practice, the directors issue shares worth up to the tax concessional limit, currently \$1,000 per eligible employee each year. The fair value of shares issued during the financial year is the market price of the Company's shares on the ASX as at the start of trading on the issue date.

Shares under the Plan vest with the employee immediately but are non-transferable for a period of up to three years. For the year ended 30 June 2016, the Company issued 16,116 shares under the Plan; see Note 6.2.

4.4 Key management personnel

The following were key management personnel (KMP) of Cochlear at any time during the financial year and unless otherwise indicated were KMP for the entire financial year:

Non-executive directors

Mr R Holliday-Smith (Chairman), Mrs YA Allen, Mr G Boreham, AM, Prof E Byrne, AC, Ms A Deans, Mr A Denver and Mr DP O'Dwyer

Executive director

Dr CG Roberts¹ and Mr C Smith²

Other executive KMP

Mr R Brook, Mr D Howitt, Mr J Janssen, Mr NJ Mitchell and Mr T Manna.

1. Retired on 31 August 2015, therefore, only a KMP from 1 July 2015 to 31 August 2015.

2. Appointed executive director on 1 September 2015 and was an other executive KMP from 1 July 2015 to 31 August 2015.

Key management personnel disclosures

The KMP compensation is included in employee expenses as follows:

	Short-term employee benefits	Post- employment benefits	Other long- term benefits	Directors' retirement benefits	Share based payments	End of service provision	Total
	\$	\$	\$	\$	\$	\$	\$
2016	10,274,302	521,446	38,969	9,586	2,794,586	-	13,638,889
2015	9,021,013	444,445	65,942	10,729	3,017,836	1,548,418	14,108,383

Information regarding individual KMP remuneration and some equity instruments disclosures as permitted by section 300A of the *Corporations Act 2001* is provided in the Remuneration Report in the Directors' Report on pages 31 to 49.

The KMP have not received any loans from Cochlear and there have been no other related party transactions with any of Cochlear's KMP.

5. Operating assets and liabilities

5.1 Inventories

Inventories are measured at the lower of cost and net realisable value.

Cost is based on the first-in-first-out principle including expenditure incurred in acquiring the inventories and bringing them to their existing condition and location. In the case of manufactured inventories and work in progress, cost includes an appropriate share of production overheads based on normal operating capacity.

Net realisable value is the estimated selling price in the ordinary course of business less estimated costs of completion and selling, marketing and distribution expenses.

	Raw materials	Work in progress	Finished goods	Total inventories
	\$000	\$000	\$000	\$000
2016	49,248	25,512	79,343	154,103
2015	40,315	20,162	85,384	145,861

5.2 Property, plant and equipment

Owned assets

The value of property, plant and equipment is measured as the cost of the asset, minus accumulated depreciation and impairment losses (see Note 5.3). The cost of the asset is the consideration provided plus incidental costs directly attributable to the acquisition.

The value of self-constructed assets includes the cost of material and direct labour and any other costs directly attributable to bringing the asset to a working condition for its intended use.

Subsequent costs in relation to replacing a part of property, plant and equipment are capitalised in the carrying amount of the item if it is probable that future economic benefits will flow to Cochlear and its cost can be measured reliably. All other costs are recognised in the income statement as incurred.

Leased assets

Payments made under operating leases are expensed on a straight-line basis over the term of the lease, except where an alternative basis is more representative of the pattern of benefits to be derived from the leased property. Minimum lease payments include fixed rate increases.

Depreciation

Depreciation is calculated to expense the cost of items of property, plant and equipment less their estimated residual values on a straight-line basis over their estimated useful lives. The estimated useful lives in the current and comparative years are as follows: leasehold improvements between one to 15 years and plant and equipment three to 14 years.

Depreciation is recognised in the income statement from the date of acquisition or, in respect of internally constructed assets, from the time an asset is completed and held ready for use.

Depreciation rates and methods, useful lives and residual values are reviewed at each balance sheet date. When changes are made, adjustments are reflected prospectively in current and future financial years only.

Total property, plant and equipment at net book value

	Leasehold improvements		Plant and equipment		Total net book value	
	2016	2015	2016	2015	2016	2015
	\$000	\$000	\$000	\$000	\$000	\$000
At cost	34,657	32,325	193,401	193,703	228,058	226,028
Accumulated depreciation	(21,774)	(20,941)	(119,406)	(124,278)	(141,180)	(145,219)
Net book value	12,883	11,384	73,995	69,425	86,878	80,809

Reconciliations of the carrying amounts are:

Opening balance	11,384	7,947	69,425	67,829	80,809	75,776
Additions	3,930	4,796	24,928	19,101	28,858	23,897
Disposals	(185)	-	(3,398)	(617)	(3,583)	(617)
Depreciation	(2,359)	(1,867)	(17,508)	(18,005)	(19,867)	(19,872)
Effect of movements in foreign exchange	113	508	548	1,117	661	1,625
Net book value	12,883	11,384	73,995	69,425	86,878	80,809

5.3 Intangible assets

Goodwill

All business combinations are accounted for by applying the acquisition method. Goodwill represents the difference between the cost of the acquisition and the fair value of the net identifiable assets acquired.

Goodwill is stated at cost less any accumulated impairment losses. Goodwill is tested annually for impairment.

Enterprise resource planning system

System costs are recognised as an intangible asset where Cochlear controls future economic benefits as a result of the costs incurred, and are stated at cost less accumulated amortisation. Costs include expenditure directly related to the development and implementation (hardware and software costs) of the system including direct labour.

Other intangible assets

Other intangible assets, comprising acquired technology, patents and licences, customer relationships, capitalised development expenditure and intellectual property, are acquired individually or through business combinations and are stated at cost less accumulated amortisation and impairment losses (see below).

Both customer relationships and capitalised development expenditure had a written down value of nil as at 30 June 2016.

Amortisation

Amortisation is calculated to expense the cost of intangible assets less their estimated residual values on a straight-line basis over their estimated useful lives. The estimated useful lives for the current and comparative years are as follows: acquired technology, patents and licences are between four to 15 years and enterprise resource planning system between two to seven years.

Amortisation is recognised in the income statement from the date the assets are available for use unless their lives are indefinite.

Goodwill and intangible assets with an indefinite useful life are systematically tested for impairment annually.

	Intangible assets with indefinite useful life		Intangible assets with finite useful life			Intangible assets
	Goodwill	Technology relationship	Enterprise resource planning system	Acquired technology, patents and licences	Other intangible assets	Total
	\$000	\$000	\$000	\$000	\$000	\$000
2016						
At cost	171,356	1,800	56,880	65,322	16,966	312,324
Accumulated amortisation	-	-	(33,929)	(37,848)	(16,209)	(87,986)
Net book value	171,356	1,800	22,951	27,474	757	224,338
Reconciliations of the carrying amounts are:						
Opening balance	170,503	1,800	25,859	29,308	1,061	228,531
Acquisitions	-	-	7,556	1,140	-	8,696
Amortisation	-	-	(10,353)	(2,972)	(299)	(13,624)
Effect of movements in foreign exchange	853	-	(111)	(2)	(5)	735
Net book value	171,356	1,800	22,951	27,474	757	224,338
2015						
At cost	170,503	1,800	73,278	64,110	16,936	326,627
Accumulated amortisation	-	-	(47,419)	(34,802)	(15,875)	(98,096)
Net book value	170,503	1,800	25,859	29,308	1,061	228,531
Reconciliations of the carrying amounts are:						
Opening balance	170,259	1,800	28,243	32,498	1,315	234,115
Acquisitions	-	-	4,530	-	-	4,530
Amortisation	-	-	(6,920)	(3,165)	(295)	(10,380)
Effect of movements in foreign exchange	244	-	6	(25)	41	266
Net book value	170,503	1,800	25,859	29,308	1,061	228,531

Impairment

Cochlear annually tests goodwill and other intangible assets with indefinite useful life for impairment. Other non-financial assets, other than inventories (see Note 5.1) and deferred tax assets (see Note 3.2), are tested if there is any indication of impairment or if there is any indication that an impairment loss recognised in a prior period may no longer exist or may have decreased.

Assets are impaired if their carrying value exceeds their recoverable amount. The asset's recoverable amount is estimated based on its value in use.

An asset that does not generate independent cash flows and its individual value in use cannot be estimated is tested for impairment as part of a cash generating unit (CGU).

An impairment loss is recognised in the income statement when the carrying amount of an asset or CGU exceeds its recoverable amount. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised. An impairment loss in respect of goodwill is not reversed.

Impairment tests for CGUs

Cochlear allocates goodwill and other intangible assets to CGUs based on the expected benefits that each CGU will receive from use of those assets.

The aggregate carrying amounts of goodwill allocated to each CGU are:

	Americas \$000	EMEA \$000	Asia Pacific \$000	Total \$000
2016	86,141	75,341	9,874	171,356
2015	85,540	74,918	10,045	170,503

The recoverable amount of each CGU is based on value-in-use calculations. Those calculations use five year cash flow projections based on actual operating results, the next year's budget and the mid-term business plan. Cash flows for year 6 onwards are extrapolated using a conservative terminal growth rate of 3.0% (2015: 3.0%) per annum which is consistent with long-term economic growth rates. The pre-tax discount rate for each CGU is as follows: Americas 13.7% (2015: 14.7%), EMEA 12.4% (2015: 12.3%) and Asia Pacific 13.9% (2015: 14.1%).

The key assumptions and the approach to determining their value in the current year are:

Assumption	How determined
Discount rate	Based on weighted average cost of capital reflecting current market assessments of the time value of money and risks specific to the CGU.
Sales volume growth rate	Based on a five year cash flow projection taking into account historical growth rates and product lifecycle.
Terminal value growth rate	Based on a five year cash flow projection taking into account historical growth rates and product lifecycle.

The recoverable amount of each CGU including unallocated corporate assets is in excess of the carrying amount and therefore no impairment charge was required. The excess of recoverable amount over carrying amount is such that a reasonably possible change in assumptions is unlikely to reduce the recoverable amount below the carrying amount.

5.4 Investments

The available for sale equity securities were acquired during 2016. These assets are initially measured at fair value, plus any directly attributable transaction costs. Subsequent to initial recognition, they are measured at fair value and changes therein, other than impairment losses which are recognised in the income statement, are recognised in other comprehensive income and accumulated in the fair value reserve. When these assets are derecognised, the gain or loss accumulated in equity is reclassified to profit or loss.

5.5 Provisions

A provision is recognised in the balance sheet when:

- Cochlear has a present obligation (legal or constructive) as a result of a past event;
- a reliable estimate can be made of the amount of the obligation; and
- it is probable that an outflow of economic benefits will be required to settle the obligation.

Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risk specific to the liability.

2016	Warranties \$000	Legal and insurance \$000	Product recall \$000	Make good lease costs \$000	Patent dispute \$000	Total \$000
Opening balance	25,573	5,012	15,918	2,210	21,333	70,046
Provision made	45,759	2,607	-	164	-	48,530
Provision used	(34,999)	(3,228)	(2,898)	(67)	-	(41,192)
Effect of movements in foreign exchange	271	10	-	37	-	318
Total provisions	36,604	4,401	13,020	2,344	21,333	77,702
Represented by:						
Current	26,101	4,401	3,173	-	-	33,675
Non-current	10,503	-	9,847	2,344	21,333	44,027
Total provisions	36,604	4,401	13,020	2,344	21,333	77,702

Warranties

A provision for warranty claims is recognised in relation to sales made prior to the reporting date, based on historical claim rates and respective product populations. Warranty periods on hardware products extend for three to 10 years.

Legal and insurance

Self-insurance

Cochlear self-insures to manage certain risks associated with operating in its line of business. Claims are recognised when an incident occurs that may give rise to a claim. They are measured at the cost that Cochlear expects to incur in settling the claims, discounted using a rate that reflects current market assessments of the time value of money and the risks specific to the liability.

Product recall

On 11 September 2011, the Company initiated a worldwide voluntary recall of its unimplanted Nucleus CI500 cochlear implant range. Management has made judgements, estimates and assumptions related to probable costs arising from the recall which affect the reported amounts of assets, liabilities, income and expenses. Actual outcomes may differ from these estimates as further information is identified.

No amount has been recognised as a charge or released as a credit in the year ended 30 June 2016.

Make good lease costs

Cochlear has a number of operating leases over its offices that require the premises to be returned to the lessor in their original condition. The operating lease payments do not include an element for the repairs and overhauls.

Patent dispute

In a trial of the patent infringement lawsuit by the Alfred E. Mann Foundation for Scientific Research and Advanced Bionics LLC in January 2014, a Jury found that Cochlear Limited and its US subsidiary Cochlear Americas infringed four claims across two patents, the infringement was "willful" and awarded USD 131,216,325 in damages.

On 1 April 2015, a Judge in the United States District Court in Los Angeles, California held that three of the four patent claims were invalid and Cochlear's infringement of the remaining claim was not "willful". The Judge overturned the damages awarded because three of the four claims were held to be invalid. On 21 April 2015, the Court entered Judgment on liability only and stayed a new trial on damages pending the outcome of the appeals by all parties from the Judgment to the United States Court of Appeals for the Federal Circuit. Oral argument before a panel of Federal Circuit judges was held on 7 July 2016 and a decision on all appeals is expected during financial year 2017.

As the patents have expired, the trial Judgment and the Court of Appeals decision will not disrupt Cochlear's business or customers in the United States.

The directors have obtained external advice and are of the opinion that the facts and the law do not support the District Court's decision on infringement of the one remaining claim.

The nature of the above legal process is such that final future outcomes are uncertain. The directors have made judgements and assumptions relating to their best estimate of the outcome of this litigation and actual outcomes may differ from the estimated liability.

A provision was expensed in the half year ended 31 December 2013 in relation to this dispute. No additional amount has been provided since that initial provision. For the purpose of determining this provision, Cochlear considered its independent damages expert's assessment prepared for the trial to estimate the liability that could result from the dispute.

5.6 Contingent liabilities

The details of contingent liabilities are set out below. The directors are of the opinion that provisions are either adequate or are not required in respect of these matters, as it is either not probable that a future sacrifice of economic benefits will be required, or the amount is not capable of reliable measurement.

Product liability claims

Cochlear is currently and/or is likely from time to time to be involved in claims and lawsuits incidental to the ordinary course of business, including claims for damages relating to its products and services.

In addition, Cochlear has received legal claims and lawsuits in various countries including the United States by recipients who have had Cochlear implant CI500 series devices stop functioning for the reason that led to the September 2011 voluntary recall of unimplanted CI500 series devices.

Cochlear carries product liability insurance and has made claims under the policies. The insurers have agreed to indemnify Cochlear in accordance with the terms and conditions of the policies including deductibles and exclusions. In the opinion of the

directors, the details of the product liability insurance policies are commercially sensitive and any disclosure of these details may be prejudicial to the interests of Cochlear.

6. Capital and financial structure

6.1 Capital management

Cochlear's capital management objectives are to safeguard its ability to continue as a going concern, provide returns to shareholders, provide benefits to other stakeholders and maintain an optimal capital structure to reduce the cost of capital.

The Board aims to maintain and develop a capital base appropriate to Cochlear's objectives and monitors a number of qualitative metrics as follows:

- net gearing ratio – defined as net debt as a proportion of net debt plus total equity;
- dividend payout ratio – defined as dividends as a proportion of net profit after tax for a given period;
- growth in EPS – defined as the compound annual growth percentage in EPS over a three year period; and
- TSR – defined as the percentage growth in share price over a three year period plus the cumulative three year dividend return calculated against the opening share price in the same three year period.

Senior management tracks, manages and reports against these capital management metrics periodically as part of broader corporate governance responsibilities. The Board undertakes periodic reviews to assess whether the metrics continue to be appropriate and whether the capital management structure is appropriate to meet Cochlear's medium and long-term strategic requirements.

In order to maintain or adjust the capital structure, Cochlear may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or sell assets to reduce debt.

Neither the Company nor any of its subsidiaries is subject to externally imposed capital requirements. There were no significant changes in Cochlear's approach to capital management during the year.

Cochlear's net gearing ratio was as follows:

	Note	2016 \$000	2015 \$000
Net debt	6.3	117,821	140,503
Total equity		448,557	355,386
Net gearing ratio at 30 June		21%	28%

6.2 Capital and reserves

Share capital

The Company does not have authorised capital or par value in respect of its issued shares.

	Number of issued shares in market circulation		Number of shares held in Trust		Total number of issued shares	
	2016	2015	2016	2015	2016	2015
On issue 1 July – fully paid	56,957,274	56,937,519	124,501	124,501	57,081,775	57,062,020
Issued for nil consideration under Employee Share Plan	16,116	19,755	-	-	16,116	19,755
Issued from the exercise of options	106,746	-	-	-	106,746	-
Options vesting from Trust	88,098	-	(88,098)	-	-	-
Performance shares vesting from Trust	31,030	-	(31,030)	-	-	-
On issue 30 June – fully paid	57,199,264	56,957,274	5,373	124,501	57,204,637	57,081,775

During 2016, Cochlear purchased 134,041 shares on market to satisfy exercise of options.

Cochlear has also issued shares to employees under the Employee Share Plan (see Note 4.3).

Ordinary shares are classified as equity and incremental costs directly attributable to the issue of ordinary shares and share options are recognised as a deduction from equity, net of any income tax benefit.

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at shareholders' meetings.

Repurchase of share capital (treasury shares)

When share capital recognised as equity is repurchased, the amount of the consideration paid, including directly attributable costs, is recognised as a deduction from equity, net of any tax effects. Shares purchased by the Trust are classified as treasury shares and are presented as a deduction from total equity. When treasury shares are subsequently sold or reissued, the amount received is recognised as an increase in equity, and the surplus or deficit on the transaction is transferred to or from the share based payment reserve.

Treasury reserve

The treasury reserve comprises the cost of shares acquired by the Trust at the date of purchase.

Translation reserve

The translation reserve records the foreign currency differences arising from the translation of the financial statements of foreign operations as well as from the translation of liabilities that hedge the Company's net investment in a foreign subsidiary, where their functional currency is different to the presentation currency of the reporting entity. See Note 1.2(d) for further details.

Hedging reserve

The hedging reserve comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments related to underlying transactions that have not yet occurred.

Share based payment reserve

The share based payment reserve comprises the cost of shares, options, performance shares and performance rights granted to eligible executives under the CELTIP and CEIP, as detailed in Note 4.3 less any payments made to meet Cochlear's obligations through the acquisition of shares on market, together with any deferred tax asset/liability on such payments.

6.3 Net debt and finance costs

(a) Net debt

Loans and borrowings are recognised initially at fair value less attributable transaction costs. Subsequently, loans and borrowings are stated at amortised cost, with any difference between amortised cost and redemption value being recognised in the income statement over the period of the borrowings on an effective interest rate basis.

Debt establishment costs are capitalised and recognised as a reduction in loans and borrowings. They are recorded initially at cost and are amortised over the period of the loan. Included within loans and borrowings is an amount of \$739,755 (2015: \$448,093) in relation to unamortised loan establishment fees.

	Note	2016 \$000	2015 \$000
Loans and borrowings:			
Current		3,978	168,159
Non-current		189,260	44,552
Total loans and borrowings		193,238	212,711
Less: Cash and cash equivalents	2.7(a)	(75,417)	(72,208)
Net debt		117,821	140,503

(b) Financing arrangements

	Multi-option bank facilities			Other credit facilities		
	Secured bank loan \$000	Standby letters of credit \$000	Bank guarantees \$000	Unsecured bank overdrafts \$000	Secured bank loan \$000	Bank guarantees \$000
2016						
Utilised at reporting date	190,000	6,916	2,133	-	3,978	1,393
Not utilised at reporting date	155,000	10,951	-	299	1,989	222
Total facilities	345,000	17,867	2,133	299	5,967	1,615
2015						
Utilised at reporting date	210,000	4,926	2,218	-	3,159	1,370
Not utilised at reporting date	135,000	12,856	-	292	1,579	224
Total facilities	345,000	17,782	2,218	292	4,738	1,594

Multi-option bank facilities - Secured bank loan

Cochlear has two bank loan facilities. The first was amended and extended in June 2013 for a period of three years and a total commitment limit of AUD 200.0 million. In December 2013, the total commitment limit was increased to AUD 250.0 million. The facility has an option to allocate a letter of credit sub-facility limit of up to AUD 30.0 million for the purpose of drawing either letters of credit or bank guarantees. This letter of credit sub-limit currently is AUD 5.0 million. This facility was extended in June 2016 for a further three year period to 14 June 2019.

In June 2013, Cochlear negotiated a second loan facility for a period of five years. The facility has a total commitment limit of AUD 115.0 million, made up of an AUD 100.0 million loan sub-facility limit and incorporates an AUD 15.0 million letter of credit facility that was negotiated in August 2011.

Both facilities are secured by interlocking guarantees provided by certain controlled entities. Interest on the facilities is variable and charged at prevailing market rates.

Other credit facilities

Unsecured bank overdrafts

Certain unsecured bank overdrafts are payable on demand and are subject to annual review. Interest on unsecured bank overdrafts is variable and is charged at prevailing market rates.

Secured bank loan

Cochlear has a Japanese yen (JPY) 450.0 million loan facility. It is secured by a letter of guarantee and reviewed annually. Interest is charged at prevailing market rates.

Bank guarantees

As at 30 June 2016, Cochlear had additional contingent liability facilities denominated in United States dollars (USD), Euros (EUR), Sterling (GBP), Indian rupees and New Zealand dollars totalling AUD 1.6 million (2015: AUD 1.6 million).

(c) Finance costs

Interest income is recognised as it accrues in the income statement. Borrowing costs are recognised as they accrue in the income statement as a finance expense.

6.4 Financial risk management

The activities of Cochlear are exposed to a variety of risks, including market risk (comprising currency and interest rate risk), credit risk and liquidity risk. Cochlear's overall risk management program considers the unpredictability of financial markets and seeks to appropriately manage the potential adverse effects on financial performance.

The Board of directors has overall responsibility for the establishment and oversight of the Risk Management Framework. Under instruction of the Board, management has established a Risk Management Committee which is responsible for identifying, assessing and appropriately managing risk throughout Cochlear. Key risks are reported to the Audit Committee on a regular basis.

A Treasury Management Committee has been established to administer aspects of risk management involving currency exposure, cash and funding, to manage the impact of short-term fluctuations on Cochlear's earnings.

The Audit Committee oversees how management monitors compliance with Cochlear's Risk Management Framework, policies and procedures and is assisted by Internal Audit which undertakes reviews of key management controls and procedures.

(a) Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates and equity prices will affect Cochlear's net profit or the value of its holdings of financial instruments.

The objective of market risk management is to manage and control market risk exposures by buying and selling forward exchange contracts and incurring financial liabilities, within acceptable parameters, whilst optimising the return, all in accordance with the treasury risk policy.

Currency risk

Cochlear is exposed to currencies other than the respective functional currencies of the controlled entities, primarily AUD, USD, EUR, GBP, Swedish kroner (SEK), JPY and Swiss francs (CHF).

Over 90% of Cochlear's revenues and over 50% of costs are denominated in currencies other than AUD. Currency risk is hedged in accordance with the treasury risk policy. Risk resulting from the translation of assets and liabilities of foreign operations into Cochlear's reporting currency is not hedged.

Cochlear's exposure to foreign currency risk in relation to non-derivative financial instruments was as follows, based upon notional amounts:

Amounts local currency/thousands	USD	EUR	GBP	SEK	JPY	CHF
30 June 2016						
Trade receivables	72,845	46,439	5,818	6,690	752,963	616
Secured bank loan	-	-	-	-	(300,000)	-
Trade payables	(13,234)	(5,348)	(5,025)	(63,160)	(63,133)	(2,219)
Gross balance sheet exposure	59,611	41,091	793	(56,470)	389,830	(1,603)
30 June 2015						
Trade receivables	64,746	47,484	6,824	10,384	670,937	881
Secured bank loan	-	-	-	-	(300,000)	-
Trade payables	(14,535)	(4,657)	(5,029)	(58,466)	(87,752)	(2,446)
Gross balance sheet exposure	50,211	42,827	1,795	(48,082)	283,185	(1,565)

Derivative assets and liabilities - Forward exchange contracts

In order to reduce the impact of short-term fluctuations on Cochlear's earnings, Cochlear enters into forward exchange contracts to hedge anticipated sales and purchases in USD, EUR and JPY. The amounts of forward cover taken are in accordance with approved policy and internal forecasts.

In the year ended 30 June 2016, Cochlear designated all forward exchange contracts as cash flow hedges. These are hedges of forecast future transactions to manage the currency risk arising from exchange rate fluctuations. The hedged items were highly probable foreign currency transactions.

At the start of a hedge relationship, Cochlear designates and documents the relationship between the hedging instrument and hedged item. This includes identification of the hedging instrument, the hedged item or transaction, the nature of the risk being hedged and how Cochlear will assess the effectiveness of the hedging relationship. Cochlear regularly assesses whether the hedging instruments are expected to be highly effective in offsetting the changes in the cash flows of the respective hedged items.

Forward exchange contracts are recognised initially at fair value. Subsequently, forward exchange contracts are measured at fair value. Changes in the fair value are recognised directly in equity to the extent that the hedge is effective. The ineffective part of any hedging instrument is recognised immediately in the income statement.

If the forward exchange contract no longer meets the criteria for hedge accounting, expires or is sold, terminated or exercised, then hedge accounting is discontinued prospectively. The cumulative gain or loss previously recognised in equity remains there until the forecast transaction occurs or when cash flows arising from the transaction are received.

For cash flow hedges, the associated cumulative gain or loss is removed from equity and recognised in the income statement in the same period the hedged forecast transaction affects the income statement and on the same line item as that hedged forecast transaction.

For the year ended 30 June 2016, all cash flow hedges were effective at the reporting date.

The following table sets out the gross value to be received (sell) under forward exchange contracts and the weighted average contracted exchange rates of outstanding contracts:

	Weighted average rate	< 1 year \$000	1 - 2 years \$000	2 - 5 years \$000
30 June 2016				
Sell USD	0.74	195,817	117,236	23,468
Sell EUR	0.64	188,358	109,493	27,203
Sell JPY	83.76	12,210	6,575	1,359
30 June 2015				
Sell USD	0.84	164,538	91,800	27,079
Sell EUR	0.67	151,143	87,390	24,167
Sell JPY	89.17	10,335	5,392	1,447

It is estimated that a general increase of 10 percent in the value of the AUD against other foreign currencies would have decreased Cochlear's profit for the year ended 30 June 2016, including hedging results and after income tax, by approximately \$8.5 million (2015: \$2.3 million) and decreased Cochlear's equity by \$51.8 million (2015: \$16.6 million). A 10 percent general decrease in the value of the AUD against other foreign currencies would have increased Cochlear's profit by \$12.2 million (2015: \$8.1 million) and increased equity by \$50.2 million (2015: \$11.6 million).

The following significant exchange rates applied to Cochlear during the year:

AUD 1 =	Average rate		Reporting date spot rate	
	2016	2015	2016	2015
USD	0.729	0.844	0.740	0.766
EUR	0.658	0.697	0.669	0.686
GBP	0.494	0.532	0.557	0.487
SEK	6.141	6.483	6.285	6.367
JPY	85.089	95.725	75.410	94.969

Interest rate risk

Cochlear is exposed to interest rate risks in Australia and Japan. See Note 6.4(c) for effective interest rates, repayment and repricing analysis of outstanding debt.

At the reporting date, the interest rate profile of Cochlear's interest-bearing financial instruments is financial assets of \$75.4 million (2015: \$72.2 million) and financial liabilities of \$193.2 million (2015: \$212.7 million).

For the year ended 30 June 2016, it is estimated that a general increase of one percent in interest rates would have decreased Cochlear's profit after income tax and equity by approximately \$1.1 million (2015: \$1.3 million). A one percent general decrease in interest rates would have had the equal but opposite effect on Cochlear's profit and equity.

(b) Credit risk

Credit risk is the risk of financial loss to Cochlear if a customer or counterparty to a financial instrument fails to meet its contractual obligations. Cochlear is exposed to credit risk from its operating activities (primarily from trade and other receivables) and from financing activities, including deposits with financial institutions and foreign exchange contracts. The carrying amounts of these financial assets at year end represent Cochlear's maximum exposure to credit risk.

Credit risk management - Trade and other receivables

Customer credit risk is managed at a regional level, subject to Board approved policies and procedures. The ageing profile of total receivables balances, individually significant debtors by geographic region, high risk customers and collection activities are reported to management and the Board of directors on a monthly basis. Where high risk customers are identified, regional management is responsible for placing restrictions on future trading, including suspending future shipments and administering dispatches on a prepayment basis.

Cochlear's exposure to credit risk is influenced mainly by the geographical location and characteristics of individual customers. Cochlear does not have a significant concentration of credit risk with a single customer.

The maximum exposure to credit risk for trade receivables at the reporting date by geographic region was:

	Americas	EMEA	Asia Pacific	Total
	\$000	\$000	\$000	\$000
2016	86,115	108,937	73,486	268,538
2015	74,153	108,374	54,201	236,728

Depending on the region, Cochlear's credit terms are generally 30 days; however, there are certain jurisdictions where it is customary practice for customers to make payment beyond 270 days. Although Cochlear discloses the balance as overdue, it is not indicative of a higher than normal credit risk as payments are typically received by Cochlear within the extended timeframes.

At each reporting date, Cochlear assesses the collectability of trade and other receivables by reference to historical collection trends and timing of recoveries and makes an adjustment if current economic and credit conditions are such that the actual losses are likely to be greater or lesser than suggested by historical trends.

Cochlear has established an allowance for impairment that represents its estimate of incurred losses in respect of trade receivables based on individually significant exposures, a collective loss component established for groups of assets meeting certain ageing profiles and customer types which have been assessed as impaired under Cochlear's accounting policy.

Based upon past experience, Cochlear believes that no impairment allowance is necessary in respect of trade receivables not past due.

Trade and other receivables are stated at amortised cost less impairment losses. The ageing of Cochlear's trade receivables at the reporting date was:

	2016	2015
	\$000	\$000
Trade receivables		
Not past due	199,164	162,018
Past due 1 – 60 days	33,162	26,644
Past due 61 – 180 days	13,469	25,315
Past due 181 – 360 days	14,924	13,252
Past due 361 days and over	19,749	15,192
	280,468	242,421
Impairment losses	(11,930)	(5,693)
Trade receivables net of allowance for impairment losses	268,538	236,728
Other receivables – current	13,387	13,016
Trade and other receivables	281,925	249,744

Credit risk management - Cash deposits and forward exchange contracts

The majority of Cochlear's cash deposits and all hedging transactions are only executed with leading financial institutions whose credit rating is at least A on the Standard & Poor's rating index.

(c) Liquidity risk

Liquidity risk is the risk that Cochlear will not be able to meet its financial obligations as they fall due. Cochlear manages liquidity risk by ensuring, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due.

Non-derivative liabilities

Contractual maturities of non-derivative financial liabilities, including estimated interest payments and excluding the impact of netting agreements, are as follows:

	Effective interest rate Per annum	Carrying amount \$000	Contractual cash flows \$000	< 1 year \$000	1 - 2 years \$000	2 - 5 years \$000
30 June 2016						
AUD floating rate loan	3.76%	189,260	207,650	7,152	107,110	93,388
JPY floating rate loan	0.61%	3,978	3,994	3,994	-	-
Trade and other payables	-	110,354	110,354	110,354	-	-
Total		303,592	321,998	121,500	107,110	93,388
30 June 2015						
AUD floating rate loan	3.99%	209,552	221,698	173,122	1,798	46,778
JPY floating rate loan	0.64%	3,159	3,172	3,172	-	-
Trade and other payables	-	99,858	99,858	99,858	-	-
Total		312,569	324,728	276,152	1,798	46,778

It is not expected that the cash flows included in the maturity analysis could occur significantly earlier or at significantly different amounts.

Derivative assets and liabilities - Forward exchange contracts

The following table indicates the periods in which the cash flows associated with Cochlear's derivatives that are cash flow hedges are expected to occur:

	Carrying amount \$000	Contractual cash flows \$000	< 1 year \$000	1 - 2 years \$000	2 - 5 years \$000
30 June 2016					
Assets	22,167	22,634	11,573	8,642	2,419
Liabilities	(16,190)	(16,400)	(12,756)	(3,416)	(228)
Total	5,977	6,234	(1,183)	5,226	2,191
30 June 2015					
Assets	5,763	5,877	3,899	1,897	81
Liabilities	(35,123)	(35,807)	(24,422)	(9,445)	(1,940)
Total	(29,360)	(29,930)	(20,523)	(7,548)	(1,859)

The expected impact on the income statement is not considered to be significantly different to the cash flow impact noted above.

(d) Fair value

The carrying amounts and estimated fair values of Cochlear's financial assets and liabilities are materially the same.

The fair value of forward exchange contracts is based upon the listed market price, if available. If a listed market price is not available, the fair value is estimated by discounting the difference between the contractual forward price and the current forward price for the residual maturity of the contract using benchmark bill futures and swap rates. These fair values are provided by independent third parties.

Valuation of financial assets and liabilities

For financial asset and liabilities measured and carried at fair value, Cochlear uses the following levels to categorise the valuation methods used:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

All of Cochlear's forward exchange contracts were valued using observable market inputs (Level 2) and there were no transfers between levels during the year.

The equity securities classified as available for sale financial assets are valued using unobservable market inputs (Level 3). Unobservable inputs are those not readily available in an active market. These inputs are generally derived from other observable inputs that match the risk profile of the financial instruments and validated against current market assumptions and historical transactions where available.

7. Other notes

7.1 Auditors' remuneration

	2016	2015
	\$	\$
Audit services		
Auditors of the Company - KPMG:		
- audit and review of financial reports	1,583,831	1,559,738
- other regulatory compliance services	58,734	72,094
Total audit services	1,642,565	1,631,832
Non-audit services		
Auditors of the Company - KPMG:		
- taxation compliance and other services	1,051,398	988,156
Total non-audit services	1,051,398	988,156

7.2 Commitments

Operating lease commitments

Cochlear leases property under non-cancellable operating leases expiring from one to 15 years. Leases generally provide Cochlear with a right of renewal at which time all terms are renegotiated.

Future non-cancellable operating lease rentals not provided for in the financial statements are payable as follows:

	2016	2015
	\$000	\$000
Not later than one year	22,372	22,028
Later than one year but not later than five years	82,528	79,308
Later than five years	65,312	88,387
Total operating lease commitments	170,212	189,723

Capital expenditure commitments

As at 30 June 2016, Cochlear entered into contracts to purchase property, plant and equipment for \$4,426,000 (2015: \$5,408,000).

7.3 Controlled entities

Subsidiaries conduct business transactions with various controlled entities. Such transactions include purchases and sales of certain products, dividends, interest and loans.

	Interest held		Country of incorporation/ formation	
	2016 %	2015 %		
Company				
Cochlear Limited			Australia	
Controlled entities				
Acoustic Implants Limited	100	100	UK	
Cochlear AG	100	100	Switzerland	
Cochlear Americas	100	100	USA	
Cochlear Austria GmbH	100	100	Austria	
Cochlear Benelux NV	100	100	Belgium	
Cochlear Bone Anchored Solutions AB	100	100	Sweden	
Cochlear Boulder LLC	100	100	USA	
Cochlear Canada Inc	100	100	Canada	
Cochlear Clinical Services LLC	100	100	USA	
Cochlear Deutschland GmbH & Co KG	100	100	Germany	
Cochlear Employee Share Trust	100	100	Australia	
Cochlear Europe Finance GmbH	100	100	Germany	
Cochlear Europe Limited	100	100	UK	
Cochlear Executive Long Term Incentive Plan (Performance Shares) Trust	100	100	Australia	
Cochlear Finance Pty Limited	100	100	Australia	
Cochlear France SAS	100	100	France	
Cochlear German Holdings Pty Limited	100	100	Australia	
Cochlear Holdings NV	100	100	Belgium	
Cochlear Incentive Plan Pty Limited	100	100	Australia	
Cochlear Investments Pty Ltd	100	100	Australia	
Cochlear Italia SRL	100	100	Italy	
Cochlear Korea Limited	100	100	Korea	
Cochlear Latinoamerica S.A.	100	100	Panama	
Cochlear Malaysia Sdn. Bhd.	100	100	Malaysia	
Cochlear Manufacturing Corporation	100	100	USA	
Cochlear Medical Device (Beijing) Co., Ltd	100	100	China	
Cochlear Medical Device Company India Private Limited	100	100	India	
Cochlear Middle East FZ-LLC	100	100	UAE	
Cochlear Nordic AB	100	100	Sweden	
Cochlear NZ Limited	100	100	New Zealand	
Cochlear Research and Development Limited	100	100	UK	
Cochlear Shared Services S.A.	100	100	Panama	
Cochlear Sweden Holdings AB	100	100	Sweden	
Cochlear Tempe LLC	(i)	-	100	USA
Cochlear Tibbi Cihazlar ve Saglik Hizmetleri Limited Sirketi		100	100	Turkey
Cochlear Verwaltungs GmbH		100	100	Germany
Cochlear (HK) Limited		100	100	Hong Kong
Cochlear (UK) Limited	(ii)	100	100	UK
Isitme Implantlari Tibbi Cihazlar ve Saglik Hizmetleri Ltd Sti		100	100	Turkey
Lachlan Project Development Pty Ltd		100	100	Australia
Medical Insurance Pte Limited		100	100	Singapore
Miaki NV	(iii)	-	100	Belgium
Nihon Cochlear Co Limited		100	100	Japan

(i) Divested on 14 December 2015.

(ii) Dormant.

(iii) Deregistered during the year ended 30 June 2016.

7.4 Parent entity disclosures

At, and throughout the financial year ended, 30 June 2016, the parent company of Cochlear was Cochlear Limited.

	2016	2015
	\$000	\$000
Result of the parent entity:		
Net profit	158,544	118,597
Other comprehensive income/(loss)	24,751	(20,967)
Total comprehensive income	183,295	97,630
Financial position of the parent entity at year end:		
Current assets	392,777	387,569
Total assets	816,734	713,614
Current liabilities	141,427	306,808
Total liabilities	486,883	461,904
Total equity of the parent entity comprising:		
Issued capital	159,303	152,599
Treasury reserve	(363)	(8,463)
Translation reserve	83	69
Hedging reserve	4,189	(20,547)
Share based payment reserve	27,023	26,887
Retained earnings	139,616	101,165
Total equity	329,851	251,710

Dividend income from subsidiaries is recognised by the parent entity when the dividends are declared by the subsidiary.

Parent entity contingencies

The details of all contingent liabilities in respect to Cochlear Limited are disclosed in Note 5.6.

Parent entity capital commitments for acquisition of plant and equipment

As at 30 June 2016, the parent entity entered into contracts but had not provided for or paid to purchase plant and equipment for \$4,420,000 (2015: \$4,823,000).

7.5 Changes in accounting policies

There have been no changes to accounting standards impacting Cochlear in the current financial year.

7.6 New standards and interpretations not yet adopted

A number of new standards, amendments to standards and interpretations are effective for financial years beginning on or after 1 July 2016, and have not been applied in preparing these consolidated financial statements. Of the new standards, only the below are expected to have an effect on the consolidated financial statements of Cochlear.

Cochlear is currently assessing the impact of the changes in the below standards and it is not expected that the changes will have a significant impact on Cochlear:

- AASB 9 Financial Instruments, which becomes mandatory for Cochlear's 2019 consolidated financial statements; and
- AASB 15 Revenue from Contracts with Customers, which becomes mandatory for Cochlear's 2019 consolidated financial statements.

Cochlear is currently assessing the impact of the changes in the below standard:

- AASB 16 Leases, which becomes mandatory for Cochlear's 2020 consolidated financial statements.

Cochlear does not plan to adopt these standards early.

7.7 Events subsequent to the reporting date

Other than the matter noted below, there has not arisen in the interval between the reporting date and the date of this Financial Report, any item, transaction or event of a material and unusual nature likely, in the opinion of the directors of the Company, to significantly affect the operations of Cochlear, the results of those operations, or the state of affairs of Cochlear in future financial years:

Dividends

For dividends declared after 30 June 2016, see Note 2.6.

1. In the opinion of the directors of Cochlear Limited (the Company):

- (a) the consolidated financial statements and notes and the Remuneration Report in the Directors' Report set out on pages 31 to 49, are in accordance with the *Corporations Act 2001*, including:
- (i) giving a true and fair view of the Consolidated Entity's financial position as at 30 June 2016 and of its performance for the financial year ended on that date; and
 - (ii) complying with Australian Accounting Standards and the *Corporations Regulations 2001*; and
- (b) there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.

2. The directors have been given the declarations required by section 295A of the *Corporations Act 2001* from the Chief Executive Officer & President and Chief Financial Officer for the financial year ended 30 June 2016.

3. The directors draw attention to Note 1.2(a) to the consolidated financial statements, which includes a statement of compliance with International Financial Reporting Standards.

Signed in accordance with a resolution of the directors:

Dated at Sydney this 9th day of August 2016.



Director



Director



INDEPENDENT AUDIT REPORT to the Members of Cochlear Limited

Report on the financial report

Opinion

We have audited the accompanying financial report of Cochlear Limited (the Company), which comprises the balance sheet as at 30 June 2016, the income statement, the statement of comprehensive income, the statement of changes in equity and the statement of cash flows for the year then ended, notes 1 to 7.7, comprising a summary of significant accounting policies and other explanatory information, and the directors' declaration of the Consolidated Entity comprising the Company and the entities it controlled at the year's end or from time to time during the financial year.

In our opinion:

- (a) the accompanying financial report of the Consolidated Entity is in accordance with the *Corporations Act 2001*, including:
 - i. giving a true and fair view of the Consolidated Entity's financial position as at 30 June 2016 and of its performance for the year ended on that date; and
 - ii. complying with Australian Accounting Standards and the *Corporations Regulations 2001*.
- (b) the financial report also complies with International Financial Reporting Standards as disclosed in note 1.2(a).

Emphasis of matter

We draw attention to note 5.5 to the financial statements which describes the uncertainty related to the outcome of the lawsuit filed against the Consolidated Entity for alleged patent infringement. Our audit report is not modified in respect of this matter.

Basis for opinion

We conducted our audit in accordance with Australian Auditing Standards. Those standards require that we comply with relevant ethical requirements relating to audit engagements and plan and perform the audit to obtain reasonable assurance about whether the financial report is free from material misstatement. Our responsibilities under those standards are further described in the *Auditor's responsibility* section of our report. We are independent of the Consolidated Entity in accordance with the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's *APES 110 Code of Ethics for Professional Accountants* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

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

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial report of the current period. These matters were addressed in the context of our audit of the financial report as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key audit matter

How our audit addressed the key audit matter

Patent dispute provision \$21.3 million

Refer to note 5.5 Provisions

The patent dispute provision relates to a specific claim that has been made against the Consolidated Entity.

We focused on this area as a key audit matter due to the:

- Quantum of amounts involved; and
- Inherent uncertainty in the application of the measurement aspects of accounting standards to determine the amount, if any, to be provided for when an item is subject to dispute and a legal process between parties.

Our procedures included, amongst others:

- Making enquiries of management and the directors to obtain their view on this significant legal matter;
 - Evaluating the information held by the Consolidated Entity and assessing the impact of this evidence on the appropriateness of the provision in relation to the measurement criteria in the accounting standards;
 - Issuing requests for confirmation of all significant litigation to the Consolidated Entity's external lawyers. We assessed the correspondence received from external lawyers by comparing this to our understanding of views expressed by management and the directors, and the consistency to facts and conditions gathered across our work; and
 - Assessing the Consolidated Entity's disclosures of the quantitative and qualitative considerations in relation to the provision, by comparing these disclosures to our understanding of the matter.
-

Key audit matter

How our audit addressed the key audit matter

CI500 product recall provision \$13.0 million

Refer to note 5.5 Provisions

On 11 September 2011, the Consolidated Entity announced the voluntary recall of unimplanted Nucleus CI500 series implantable devices as a consequence of an increase in the number of Nucleus CI500 series implant failures. Certain assumptions have been made by the Consolidated Entity in providing for costs associated with the recall.

The CI500 series product recall provision was considered a key audit matter due to:

- The inherent uncertainty associated with estimating device return and claim rates, and associated future warranty claim costs;
- The inherent subjectivity in assessing the associated level of insurance cover; and
- The potentially significant amounts involved.

These conditions necessitated greater involvement by our senior team members to challenge the forward looking assumptions adopted by the Consolidated Entity in their model that determined the amount provided.

Our procedures included, amongst others:

- Assessing the key forward looking assumptions used by the Consolidated Entity in their model to estimate the provision, including estimated device return rates and estimated warranty and associated claim costs, by comparing with historical actuals;
- Assessing the impact on the provision of insurance cover by comparing the forward looking insurance recovery assumptions with historical actuals;
- Assessing correspondence from the Consolidated Entity's external lawyers in response to our requests for information on claims regarding known or alleged CI500 implant failures to assist us in challenging the CI500 provision. We compared this to our understanding of facts and conditions gathered across our work;
- Challenging the key forward looking assumptions used by the Consolidated Entity in their model to estimate the provision by performing sensitivity analysis in relation to estimated device return and claim rates, and estimated warranty and associated claim costs; and
- Assessing the Consolidated Entity's disclosures of the quantitative and qualitative considerations in relation to the provision, by comparing these disclosures to our understanding of the matter.

Recoverability of trade receivables \$268.5 million

Refer to note 6.4(b) Financial risk management, credit risk

Recoverability of trade receivables is a key audit matter due to:

- The wide ranging characteristics of individual customers;
- The large number of different geographic locations of customers;
- Some customers and locations having experienced higher days sales outstanding than the Consolidated Entity's average days sales outstanding, increasing their inherent exposure to credit risk;
- The use of non-standard and unique contracts with customers, some of which have longer than average payment terms specifically negotiated by the Consolidated Entity; and
- The inherent subjectivity involved in the Consolidated Entity making judgements in relation to credit risk exposures.

These conditions gave rise to additional audit effort to gather evidence across the unique profiles of customers and their accounts receivable, including focusing our work on those with greater credit risk exposures, whether driven from relative exposure or location characteristics.

Our procedures included, amongst others:

- Testing key controls within the credit control process including credit account application approvals and credit limit review;
- Assessing the recoverability of a sample of outstanding trade receivable balances by comparing management's views of recoverability of amounts outstanding to historical patterns of receipts, in conjunction with assessing cash received subsequent to year end for its effect in reducing amounts outstanding at year end;
- Challenging management's view of credit risk and recoverability in certain locations by selecting a sample of overdue customer balances and:
 - noting the historical patterns for long outstanding trade receivables in those locations;
 - assessing cash received subsequent to year end for its effect in reducing amounts outstanding at year end;
 - evaluating other evidence including customer correspondence; and
 - questioning management's knowledge of future conditions that may impact expected customer receipts.
- Assessing the Consolidated Entity's disclosures of the quantitative and qualitative considerations in relation to trade receivables credit risk, by comparing these disclosures to our understanding of the matter.



INDEPENDENT AUDIT REPORT to the Members of Cochlear Limited

Directors' responsibility for the financial report

The directors of the Company are responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal control as the directors determine is necessary to enable the preparation of the financial report that gives a true and fair view and is free from material misstatement, whether due to fraud or error. In note 1.2(a), the directors also state, in accordance with Australian Accounting Standard AASB 101 Presentation of Financial Statements, that the financial report complies with International Financial Reporting Standards.

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

Auditor's responsibility

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

As part of an audit in accordance with Australian Auditing Standards, we exercise professional judgement and maintain professional scepticism throughout the audit.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial report.

The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial report, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation of the financial report that gives a true and fair view in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control.

The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial report.

We conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Consolidated Entity's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial report or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Consolidated Entity to cease to continue as a going concern.

We evaluate the overall presentation, structure and content of the financial report, including the disclosures, and whether the financial report represents the underlying transactions and events in a manner that achieves fair presentation.

We obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Consolidated Entity to express an opinion on the financial report. We are responsible for the direction, supervision and performance of the Consolidated Entity audit. We remain solely responsible for our audit opinion.



INDEPENDENT AUDIT REPORT to the Members of Cochlear Limited

We communicate with the directors regarding, amongst other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

The Auditing Standards require that we comply with relevant ethical requirements relating to audit engagements. We also provide the directors with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with the directors, we determine those matters that were of most significance in the audit of the consolidated financial report of the current period and are therefore key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Report on the remuneration report

We have audited the Remuneration Report included in pages 31 to 49 of the Directors' Report for the year ended 30 June 2016. The directors of the Company are responsible for the preparation and presentation of the Remuneration Report in accordance with Section 300A of the *Corporations Act 2001*. Our responsibility is to express an opinion on the Remuneration Report, based on our audit conducted in accordance with Australian Auditing Standards.

Opinion

In our opinion, the Remuneration Report of Cochlear Limited for the year ended 30 June 2016, complies with Section 300A of the *Corporations Act 2001*.

KPMG
Sydney, 9 August 2016

Cameron Slapp, Partner

ADDITIONAL INFORMATION

Additional information required by Australian Securities Exchange Listing Rules and not disclosed elsewhere in this report – the information presented is as at 29 July 2016:

Shareholdings

Substantial investors

Investor	Number of ordinary shares	%
Baillie Gifford & Co	6,019,800	10.52
Hyperion Asset Management Limited	2,861,780	5.00
Total	8,881,580	15.52

Distribution of shareholders

Number of shares held	Number of ordinary shareholders
1 - 1,000	25,556
1,001 - 5,000	2,542
5,001 - 10,000	152
10,001 - 100,000	69
100,001 and over	14
Total	28,333

Non-marketable parcels – 141 shareholders held less than a marketable parcel of ordinary shares.

Twenty largest shareholders

Shareholder	Number of ordinary shares	%
HSBC Custody Nominees (Australia) Limited	15,158,679	26.50
JP Morgan Nominees Australia Limited	10,084,945	17.63
National Nominees Limited	9,567,204	16.72
Citicorp Nominees Pty Limited	2,958,943	5.17
BNP Paribas Noms Pty Ltd (DRP)	1,701,927	2.98
AMP Life Limited	763,871	1.34
RBC Investor Services Australia Nominees Pty Limited (Bkcust a/c)	517,403	0.90
Dr Christopher Graham Roberts	396,348	0.69
BNP Paribas Nominees Pty Ltd (Agency Lending DRP a/c)	385,555	0.67
Citicorp Nominees Pty Limited (Colonial First State Inv a/c)	375,868	0.66
HSBC Custody Nominees (Australia) Limited – a/c 2	295,460	0.52
HSBC Custody Nominees (Australia) Limited (NT-Comnwlth Super Corp a/c)	287,366	0.50
RBC Investor Services Australia Nominees Pty Ltd (Bkmini a/c)	132,400	0.23
PGA (Investments) Pty Ltd	100,000	0.17
RBC Investor Services Australia Pty Limited (VFA a/c)	100,000	0.17
National Nominees Limited (DB a/c)	77,361	0.14
Australian Foundation Investment Company Limited	75,000	0.13
Share Direct Nominees Pty Ltd (10015 a/c)	74,594	0.13
HSBC Custody Nominees (Australia) Limited	72,518	0.13
Navigator Australia Ltd (MLC Investment Sett a/c)	53,954	0.09
		75.47

The 20 largest shareholders held 75.47% of the ordinary shares of the Company.

Glossary, Key Company ASX Announcement Record and Company Information

Glossary

AGM Annual General Meeting.	FY15 Financial year 2015: 1 July 2014 to 30 June 2015.
ASIC Australian Securities & Investments Commission.	FY16 Financial year 2016: 1 July 2015 to 30 June 2016.
ASX Australian Securities Exchange.	FY17 Financial year 2017: 1 July 2016 to 30 June 2017.
EBIT Earnings before interest and tax.	FDA United States Food and Drug Administration.
EBITDA Earnings before interest, tax, depreciation and amortisation.	FX Foreign exchange.
EMEA Europe, Middle East and Africa.	IFRS International Financial Reporting Standards.
EPS Earnings per share.	KMP Key management personnel.
FY11 Financial year 2011: 1 July 2010 to 30 June 2011.	Processor/sound processor The externally worn part of the cochlear implant.
FY12 Financial year 2012: 1 July 2011 to 30 June 2012.	R&D Research and development.
FY13 Financial year 2013: 1 July 2012 to 30 June 2013.	STEM Science, Technology, Engineering and Mathematics.
FY14 Financial year 2014: 1 July 2013 to 30 June 2014.	TSR Total shareholder return.

Key Company ASX Announcement Record

11 August 2015

Full year results for year ended 30 June 2015

Cochlear announced that sales revenue increased 15% to \$941.9 million on the previous financial year. Total dividends for the year were \$1.90, 71% franked, a decrease of 25% on the prior year.

31 August 2015

CEO handover effective

Cochlear confirmed the appointment of Chief Executive Officer & President Chris Smith effective from 1 September 2015. He was appointed as an Executive Director from that same date.

20 October 2015

AGM Chairman's address

Cochlear Chairman, Rick Holliday-Smith, addressed shareholders at the Annual general Meeting.

11 February 2016

Half year results announced

Cochlear announced that sales revenue increased 32% to \$581.7 million on the previous half year. An interim dividend of \$1.10 was declared, 100% franked, and an increase of 22% on the prior half.

28 April 2016

Cochlear hosts investor day

Cochlear hosted an investor day for institutional shareholders and analysts with presentations made by senior management across a number of areas of the business.

Non-IFRS financial measures

Given the significance of the patent dispute, 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 patent dispute provision: IFRS measures adjusted for the expense of the patent dispute provision;
- excluding product recall costs: IFRS measures adjusted for the costs of the product recall; and
- constant currency: restatement of IFRS financial measures in comparative years using FY16 FX rates.

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

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 18 October 2016 at the Australian Securities Exchange, Exchange Square Auditorium, 20 Bridge Street, Sydney.

Financial calendar

2016

Dividend record date 8 September
Payment of final dividend 29 September
Annual General Meeting 18 October

2017

Interim profit announcement 14 February*
Interim dividend record date 16 March*
Payment of interim dividend 6 April*
Final profit announcement 17 August*
Annual General Meeting 17 October*

* Indicative dates only.

ACE, Advance Off-Stylet, AOS, AutoNRT, Autosensitivity, Beam, Button, Carina, Cochlear, コクレア, Codacs, Contour, Contour Advance, Custom Sound, ESPrit, Freedom, Hear now. And always, Hugfit, Hybrid, inHear, Invisible Hearing, MET, MP3000, myCochlear, NRT, Nucleus, 科利耳, Off-Stylet, SmartSound, Softip, SPrint, True Wireless, the elliptical logo and Whisper are either trademarks or registered trademarks of Cochlear Limited. Ardium, Baha, Baha SoftWear, BCDrive, DermaLock, EveryWear, Vistafix and WindShield are either trademarks or registered trademarks of Cochlear Bone Anchored Solutions AB.

Design

Cross Media Communications Pty Ltd

Hear now. And always

As the global leader in implantable hearing solutions, Cochlear is dedicated to bringing the gift of sound to people with moderate to profound hearing loss. We have helped over 400,000 people of all ages live full and active lives by reconnecting them with family, friends and community.

We give our recipients the best lifelong hearing experience and access to innovative future technologies. For our professional partners, we offer the industry's largest clinical, research and support networks.

That's why more people choose Cochlear than any other hearing implant company.