



2010 ANNUAL REPORT

**Global Competence**  
**Local Presence**

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## CHAIRMAN'S LETTER

Dear SomnoMed Shareholder,

The financial year 2009/10 was a milestone year for SomnoMed Limited. After years of generating significant losses, SomnoMed recorded in the 12 month period to June 2010, pre tax and after tax profits.

This comes as the result of year by year continuous significant improvements and consistent:

- solid growth of our SomnoDent<sup>®</sup> sales in all regions of the world;
- strong growth of revenues despite adverse currency movements;
- improving gross margins; and
- well contained and controlled expenses for central overheads and R&D.

Looking at the financial result of 2009/10 it is important to understand that the profits generated during last financial year came after absorbing:

- start up cost of our new production facility in the Philippines;
- market development expenses in Japan;
- expenses for product development and clinical testing as well as new project development; and
- sponsored clinical research in a number of countries.

The results achieved in 2009/10 are a credit to our management at our head office in Sydney, as well as our offices in Asia, Europe and the United States. I would like to take this opportunity to thank all our staff around the world for their hard work and the progress made in establishing SomnoMed as a meaningful global medical device company.

SomnoMed is positioning itself as the global leader in Dental Sleep Medicine - treating medical and dental conditions resulting from obstructive sleep apnea, snoring and bruxism (teeth grinding) during sleep. Leadership comes with an obligation to continuously support clinical research, improve existing products, and launch new and innovative concepts and products. This is what will become the main theme for SomnoMed in 2010/11.

SomnoMed is looking into the future with great confidence, given the enormous number of people suffering from the above conditions, its potential to treat these patients in a compliant, most patient friendly and effective manner and its global leadership in innovative Dental Sleep Medicine.

Finally, allow me to thank you our shareholders, for your loyalty and support in making this exciting journey with us. Directors, management and staff are fully committed to build a company we can all be proud of, and hope you will continue to accompany us on this journey.

Yours faithfully,



Peter Neustadt  
Chairman

## CHIEF EXECUTIVE OFFICER'S REPORT

Dear Fellow Shareholders,

The financial year 2009/10 has shown yet another very strong performance by SomnoMed, the worldwide leading Oral Sleep Appliance company, specialising in the treatment of sleep disordered breathing. Establishing its international footprint in 20 countries, and a solid financial performance have made SomnoMed stronger, and well prepared for the future. SomnoDent<sup>®</sup>, the oral sleep apnea appliance of choice is recognised by the medical and dental fraternity, and has set the international gold standard in terms of patient comfort, treatment outcome, and compliance. A truly remarkable achievement considering the craftsmanship involved in the fabrication and customization of each appliance to the specification of each individual patient. A SomnoDent<sup>®</sup> oral sleep apnea appliance is a technician's masterpiece of its own.

Globally, a total of 19,543 units were sold, showing a growth of 59% compared to the previous year sales of 12,544 units. Sales revenue was \$10.7 million for the year, an increase of 39% over \$7.7 million in FY 08/09. The total gross margin grew by 50% from less than \$4.06 million in FY 08/09 to \$6.08 million in FY 09/10. EBITDA improved for full year to \$269,000, from an EBITDA loss of \$1.51 million in the prior year.

Corporate overheads and business development expenses, which includes research and development costs, remained stable at \$1.768 million versus \$1.786 million in FY 08/09.

An operating profit before tax of \$114,000 has been achieved for the year compared to a reported loss of \$1.802 million in the previous year. Finally, the company reported for the first time a cash flow positive result for the full year.

### SOMNOMED – GLOBAL OPERATIONS

In the financial year ended 30<sup>th</sup> June 2010, the company completed the first strategic phase of its international expansion program and now operates in 20 countries worldwide through its wholly owned subsidiaries in Australia, Singapore, Philippines, Japan, USA and Europe.

With its presence in all key strategic markets, the company is at the forefront of Dental Sleep Medicine. More than 45,000 patients worldwide are now, or have been in treatment, making the SomnoDent<sup>®</sup> oral sleep apnea appliance a market leader in its field.

### EUROPE

The European presence has been established in key strategic regions of Northern, Central and Southern Europe, and the company is well positioned to further develop and build the fast growing European markets.

The Nordic region is a key driver of this development, in particular Sweden, where the SomnoDent<sup>®</sup> MAS has become the most innovative and leading oral sleep apnea appliance, gaining a significant market share. Neighbouring countries increasingly recognise our products and excellent services, and the company is selling into nearly all Nordic countries.

Central Europe – with its Central Laboratory in Germany and distribution partners in neighbouring countries – is developing well, and has seen increasing orders from Switzerland, Germany, and in particular Holland. Since January 2010 the oral appliance treatment is fully recognised in Holland as a standard treatment option for obstructive sleep apnea. Since the second half of FY 09/10, Holland almost has more patients being treated with SomnoDent<sup>®</sup> devices each month than Australia, which comparatively took several years to develop.

It is noted that over the past 3 years Government regulated national healthcare schemes i.e. Medicare, increasingly fund or fully reimburse an oral appliance sleep apnea treatment. We are supporting clinical studies in various European countries to provide the medical evidence for the SomnoDent<sup>®</sup> therapy. The most prominent study has been initiated in June together with the Charité in Berlin. The sleep medical faculty is directly comparing the SomnoDent<sup>®</sup> MAS with a CPAP therapy, without limitation of the severity in obstructive sleep apnea, and with a particular focus on cardiovascular disease. We are proud to be part of this study as it involves not only the medical, but also the dental faculty of the Charité.

Europe is now contributing 16% of worldwide unit sales and, during the fourth quarter of FY 09/10, the European percentage of SomnoDent<sup>®</sup> worldwide sales has grown to approximately 20%. We continue to expand our management and operation in Europe and expect to achieve a profit contribution for the full year of FY 10/11.

## **NORTH AMERICA**

Also during FY 09/10, SomnoMed's business in North America has grown significantly and is contributing 68% of worldwide sales. SomnoDent<sup>®</sup> unit sales grew by more than 50% compared to the previous year. The established network of licensed manufacturing partners in the US and in Canada, together with the SomnoMed North America operation in Texas, has proven to be successful and is a solid base for our business. The SomnoMed Dental Network has grown significantly to more than 1,600 members across North America.

In June 2010 SomnoMed attended the annual event of the American Academy of Dental Sleep Medicine, as well as the annual conference SLEEP'10 in San Antonio, with more than 6,000 delegates at both conferences. It is a significant investment for the Company as we seek to bridge the gap between the dental and medical fraternity. We received significantly more attention and enquiries than in prior years, indicating that SomnoMed is becoming the partner of trust and competence for the sleep professional in obstructive sleep disordered breathing.

San Antonio was also the platform for the product introduction of the world's first Polysomnography ("PSG") Remote Controlled Mandibular Positioner ("RCMP"). The RCMP technology was invented and patented at the University Technology International ("UTI") by Dr. John Remmers. The RCMP is manipulated by a sleep technologist and controls protrusion of the mandible during a PSG study. For Dental Sleep Medical practitioners, RCMP should increase the number of oral appliance treatment prescriptions, due to increased confidence in the treatment modality achieved by laboratory based confirmation of efficacy. Additionally, RCMP replaces often expensive and/or non-sleep medical relevant diagnostic equipment. We see this product as a breakthrough technology that further establishes the relationship between dental and medical sleep professionals based on evidence and facts.

## **AUSTRALIA, NEW ZEALAND, ASIA AND JAPAN**

The operation maintained its market leadership throughout the region. With a strong base in Australia, and with further advancements in Asia and New Zealand, the business development is steady. We have achieved good geographical coverage and a solid base for ongoing future growth, with over 300 active affiliated SomnoMed Dental Network members throughout the region, plus 70 dental clinics now qualified in Japan.

The Australasian Sleep Association, strongly supported by SomnoMed, organised its second 3-day-seminar program in Melbourne during 2009, with the number of delegates attending doubling from the previous year, showing an increasing interest in this new field of Dental Sleep Medicine.

In February 2010 we opened our new base to the company's global production and technology network in the Philippines. Together with all international licensed manufacturing partners, we are well placed operationally and technically to manage and up-scale production for future growth.

## **SMH BIOMATERIAL AG**

The unique "soft lining" material SMH BFlex has raised the appliance quality and patient comfort to a new level and is used in 70% of all SomnoDent<sup>®</sup> devices fabricated for Australasia, 90% in Europe, 100% in Japan and 50% in North America, showing a significant growth and acceptance worldwide. The SMH BFlex material is exclusively available from SMH Biomaterial AG, a 50/50 joint venture between SomnoMed and the owner of all IP relating to this worldwide unique material. Product tests through Universities and clinical laboratories in Japan and Sweden have been initiated to expand the use of SMH BFlex into other dental applications. The usage of SMH BFlex has further increased with the introduction of the Sleep Bruxism product line, "SomnoBrux", earlier this year.

## **LOOKING AHEAD**

In FY 09/10 we managed to put the loss-generating start up years behind us and have proven to be able to grow profits, making SomnoMed an even stronger company. We have achieved what we promised to create – a global, dynamic business based on sustainable growth and profitability. Our worldwide presence, broadening the product base, innovation, and optimization of our global operational performance are the focal points for the next year. We shall see the operation to grow to over 100 employees worldwide, introducing breakthrough dental and medical technologies, with the next generation of SomnoDent<sup>®</sup> sleep apnea appliance in the pipeline.

## **LOOKING AHEAD (continued)**

All this cannot be achieved single-handed, it is foremost an achievement by a dedicated and hard working team of employees sharing the fascination and passion about this newly developing field of Dental Sleep Medicine. Therefore, I am taking this opportunity to thank all our employees especially, and first. I would also like to thank our loyal members of the SomnoMed Dental Network, growing in numbers worldwide year after year, and regularly reaffirming their trust in the company by choosing SomnoDent<sup>®</sup> MAS for obstructive sleep apnea treatment, or increasingly SomnoBrux for the treatment of Sleep Bruxism. In line with this development, we thank the Sleep Medical fraternity for their increasing trust in the company, and the SomnoMed Dental Network. Last but not least, a special thank you to our shareholders for their continued support and maintained confidence in the company, and its management.

It is well researched and documented that millions of people worldwide require a lifetime treatment of obstructive sleep apnea for a healthier life. A majority remain undiagnosed, but even more critical is that over 50% of all diagnosed patients remain untreated because of non-compliance with traditional treatment options. The SomnoDent<sup>®</sup> oral sleep apnea appliance offers a patented, clinically proven, and patient compliant alternative. "SomnoDent<sup>®</sup> First – Sleep, Breath, Live Better", is our slogan for FY 10/11. The multidisciplinary collaboration between the sleep medical fraternity and educated, qualified SomnoMed dentists worldwide ensure the best outcome for patient's health. At SomnoMed, the future is now.



**Ralf Barschow**  
**Chief Executive Officer**

**SOMNOMED LIMITED**  
ACN 003255221  
**DIRECTORS' REPORT**

Your directors present their report on the company and its controlled entities for the financial year ended 30 June 2010.

**Directors**

The names of directors in office at any time during or since the end of the year are:

Peter Neustadt

Graham Hurst

Paul Hopper

Directors have been in office since the start of the financial year to the date of this report, unless otherwise stated.

**Principal Activity**

The principal activity of the Consolidated Entity during the financial year was the commercialisation of the SomnoDent<sup>®</sup> MAS and other oral devices for sleep related disorders in Australia and overseas.

There were no other significant changes in the nature of the Consolidated Entity's principal activities during the financial year.

**Operating Results**

The consolidated profit of the Consolidated Entity amounted to \$786,143 (2009 loss \$1,813,673)

**Dividends Paid or Recommended**

There is no dividend paid, declared or recommended.

**Significant Changes in State of Affairs**

Other than as stated above and in the accompanying financial report, there were no significant changes in the state of affairs of the Company during the reporting year.

**After Balance Date Events**

The directors are not aware of any matter or circumstance that has arisen since the end of the year to the date of this report that has significantly affected or may affect:

- (i) The operations of the company and the entities that it controls
- (ii) The results of those operations
- (iii) The state of affairs of the Company in subsequent years.

**Future Developments**

The Company will continue to produce and sell devices for the oral treatment of sleep related disorders in Australia and overseas.

## DIRECTORS' REPORT (CONTINUED)

### Directors

#### Peter Neustadt

##### Chairman (Non-executive), Member of the Audit Committee

Dr. Peter Neustadt, born in Germany, studied in Switzerland at St.Gall Graduate School for Business & Economics, where he earned a Master in Economics (lic.oec.HSG) Doctorate in Business Administration (Dr.oec). He worked for McKinsey & Company based in Switzerland and in Mexico.

Dr Neustadt moved to Australia and joined Kerry Packer in 1980 as a member of the executive board of Consolidated Press Holdings. He was Executive Chairman and principal shareholder in diverse media group Communications & Entertainment Limited until 1987. He founded and managed resort and property group Cypress Lakes Group Limited and The Golden Door group of companies until the end of 2005. Dr Neustadt also served on the board of Channel Ten, Advance Bank, Trafalgar Properties Limited and Manboom Pty Ltd.

He is currently Chairman of mortgage and financial services group Vow Financial Holdings P/L and technology group FireWatch Australia Pty Limited. He is a member of a number of private company boards in Australia and in Europe.

#### Paul Hopper

##### Director (Non-executive)

Mr. Hopper has over 20 years international experience in the management and funding of biotechnology and healthcare public companies, and has served on the Boards of more than a dozen public companies in the US, Asia and Australia. Mr. Hopper is a Director of pSivida Corp, an ophthalmic drug delivery company completing Phase 3 clinical trials.

Mr Hopper is also a Director of Fibrocell Science Inc., which has filed a BLA with the FDA for approval of an aesthetic & cosmetic cell technology, and he is the Chairman of Viralytics Limited, which is developing an oncolytic viral vaccine. Mr. Hopper is Managing Director at the Los Angeles investment bank, Cappello Group.

#### Graham P. Hurst

##### Director (Non-executive) Chairman of the Audit Committee

Graham Hurst is an experienced investor with over forty years experience in capital markets. He became a member of the Sydney Stock Exchange in 1968 and was subsequently a director of the Sydney Stock Exchange for five years and on the Exchange's national listing committee during this time.

Graham has acted as financial advisor to a number of companies.

### Company Secretary

#### Terence Flitcroft B Comm CA FSIA

Terence has been Company Secretary since 1995.

### Board Member's Directorships

Listed below are details of other listed public company directorships held by Board Members over the last three years.

Director	Directorship of	Date Appointed	Date Resigned
Graham Hurst	Golden Tiger Mining Limited	2 November 2006	23 August 2010
Peter Neustadt	No other listed public company directorship		
Paul Hopper	Bone Medical Limited	2 June 2005	16 July 2007
	Cell Aquaculture Limited	15 August 2007	26 March 2008
	pSivida Corp	14 July 2008	Current
	Viralytics Pty Limited	4 September 2008	Current
	Fibro Science Inc.	9 September 2009	Current

## DIRECTORS' REPORT (CONTINUED)

### Directors' Interests in Securities

As at the date of this report, details of Directors who hold shares or options in the company for their own benefit or who have an interest in holdings through a third party are detailed below.

Director	Shares	Options over Ordinary Shares
Graham Hurst	791,000	50,000
Peter Neustadt *	3,371,023	125,000
Paul Hopper *	100,000	50,000

\* Held by an entity associated with the Director and in which he has a financial interest

### Meetings of Directors

The number of meetings of the Company's Board of Directors and each board committee held during the year to 30 June 2010 and the number of meetings attended by each director were:

	DIRECTORS' MEETINGS		COMMITTEE MEETINGS			
			AUDIT COMMITTEE		REMUNERATION COMMITTEE	
	Number eligible to attend	Number Attended	Number eligible to attend	Number Attended	Number eligible to attend	Number Attended
Paul Hopper	12	11	-	-	1	1
Peter Neustadt	12	12	2	2	1	1
Graham Hurst	12	11	2	2	1	1

## DIRECTORS' REPORT (CONTINUED)

### Indemnifying Directors or Officers

Each Director has entered into a Deed with the Company under which the Director is given access to documentation and in addition is:

- indemnified by the Company to the full extent permitted by law against all liabilities sustained or incurred through acting as a Director (under the Corporations Act the indemnity does not extend to a liability owed to the Company or its related bodies corporate, or which arises out of conduct involving a lack of good faith, or is for a pecuniary penalty order under section 1317G of the Corporations Act or a compensation order under section 1317H of the Corporations Act);
- indemnified by the Company to the full extent permitted by law against legal costs and expenses incurred in defending an action for a liability incurred as an officer of the Company (under the Corporations Act the indemnity does not extend to costs incurred in circumstances where the Director is found to have a liability for which the Director cannot be indemnified, or costs of defending or resisting criminal proceedings in which the Director is found guilty or defending proceedings brought by ASIC or a liquidator for a court order where the court holds that the grounds for making the order are established, or costs of proceedings seeking relief for the Director under the Corporations Act where the court denies relief);
- entitled to a loan to meet the costs of defending or responding to any such claim or proceeding; and
- entitled to have the Company maintain and pay premiums in respect of directors' and officers' insurance.

### Corporate Governance

In recognising the need for the highest standards of corporate behaviour and accountability, the directors of SomnoMed Limited support and have adhered to key principles of corporate governance. Please refer to page 15 of this annual report for more information.

### Environmental regulations

The company's operations are not materially affected by environmental regulations.

### Proceedings on Behalf of Company

No person has applied for leave of Court to bring proceedings on behalf of the company or intervene in any proceedings to which the company is a party for the purpose of taking responsibility on behalf of the company for all or any part of those proceedings.

The company was not a party to any such proceedings during the year.

## DIRECTORS' REPORT (CONTINUED)

### Options

At the date of this report the unissued ordinary shares of SomnoMed Limited under option are as follows:

Grant Dates	Date of Expiry	Exercise Price**	Number under Option**
1 May 2008	30 June 2011	\$0.60	25,000
3 September 2008	30 September 2011	\$0.72	585,000
15 October 2008	31 October 2011	\$0.80	125,000
3 September 2009	30 September 2012	\$0.58	340,000
15 October 2009	15 October 2012	\$0.58	132,500
3 September 2010	30 September 2013	\$0.99	370,000
			<b>1,577,500</b>

Options that were granted over unissued shares during or since the end of the financial year by the company to directors or any of the specified officers as part of their remuneration are detailed below:

Optionholder	Exercise price (cents)**	Options**
Ralf Barschow*	58	260,000
Ralf Barschow	99	260,000
Neil Verdal Austin	58	125,000
Chris Bedford*	58	50,000
Chris Bedford	99	50,000
John Truitt* (subsequently lapsed)	56	75,000
		<b>820,000</b>

\* Reported in previous year's Directors' Report

\*\* Adjusted for 20 for 1 consolidation of capital in November 2009

A total of 1,935,000 options have been exercised since the end of the last financial year.

A total of 240,000 options expired or lapsed since the end of the previous financial year, which were not reported in the previous year's Directors' Report.

No person entitled to exercise the option had or has any right by virtue of the option to participate in any share issue of any other body corporate.

## DIRECTORS' REPORT (CONTINUED)

### REMUNERATION REPORT

This report details the nature and amount of remuneration for each director of SomnoMed Limited and for the executives receiving the highest remuneration.

#### Remuneration Policy

The remuneration policy of SomnoMed Limited has been designed to align director and executive objectives with shareholder and business objectives by providing a fixed remuneration component and offering specific long-term incentives based on key performance areas affecting the Consolidated Entity's financial results. The board of SomnoMed Limited believes the remuneration policy to be appropriate and effective in its ability to attract and retain the best executives and directors to run and manage the Consolidated Entity, as well as create goal congruence between directors, executives and shareholders.

The following table shows the gross revenue and results for the last two years for the listed entity, as well as the share price at the end of the respective financial years.

	2010	2009
Revenue	\$10,992,000	\$8,223,570
Net profit/(loss)	\$786,143	(\$1,818,673)
Share price at year end	79.5 cents	46.0 cents*

\* Adjusted for 20 for 1 share consolidation in November 2009.

The board's policy for determining the nature and amount of remuneration for board members and senior executives of the Consolidated Entity is as follows:

The remuneration policy, setting the terms and conditions for the executive directors and other senior executives, was developed by the remuneration committee, which currently is the entire board. All executives receive a total remuneration package, which may include a base salary (commensurate with their expertise and experience), superannuation, fringe benefits, options and performance incentives. The remuneration committee reviews executive packages annually by reference to the Consolidated Entity's performance, executive performance and comparable information from industry sectors and other listed companies in similar industries.

The performance of executives is measured with each executive and is based predominantly on the forecast growth of the company financial performance and shareholders' value. All bonuses and incentives must be linked to predetermined performance criteria. Any changes must be justified by reference to measurable performance criteria. The policy is designed to attract the highest calibre of executives and reward them for performance that results in long-term growth in shareholder wealth.

Executives are also entitled to participate in the employee option arrangements.

Senior executives receive a superannuation guarantee contribution required by the government, which is currently 9%, and do not receive any other retirement benefits. Some individuals, however, have chosen to sacrifice part of their salary to increase payments towards superannuation.

All remuneration paid to directors and executives is valued at the cost to the company and expensed. Options are valued using the Black and Scholes methodology.

The board policy is to remunerate non-executive directors at market rates for comparable companies for time, commitment and responsibilities. The remuneration committee determines payments to the non-executive directors and reviews their remuneration annually, based on market practice, duties and accountability. Fees for non-executive directors are not linked to the performance of the Consolidated Entity. However, to align directors' interests with shareholder interests, the directors hold options in the company.

#### Performance Based Remuneration

As part of senior executives' remuneration packages there is a performance-based component, consisting of key performance indicators (KPIs). The intention of this program is to facilitate goal congruence between executives with that of the business and shareholders. The KPIs are set annually, with a certain level of consultation with executives. The measures are specifically tailored to the areas each executive is involved in and has a level of control over. The KPIs target areas the board believes will improve the performance of the company, covering financial and non-financial as well as short- and long-term goals. The level set for each KPI is based on budgeted figures for the group.

## DIRECTORS' REPORT (CONTINUED)

Performance in relation to the KPIs is assessed annually, with bonuses being awarded depending on the KPIs achieved. Following the assessment, the KPIs are reviewed by the Remuneration Committee in light of the desired and actual outcomes, and their efficiency is assessed in relation to the group's goals and shareholder wealth, before the KPIs are set for the following year.

In determining whether or not a KPI has been achieved, SomnoMed Limited bases the assessment on audited figures where appropriate.

### Company Performance, Shareholder Wealth and Directors' and Executives' Remuneration

The remuneration policy has been tailored to increase goal congruence between shareholders and directors and executives. There have been two methods applied in achieving this aim, the first being a performance based bonus based on key performance indicators, and the second being the issue of options to directors and executives to encourage the alignment of personal and shareholder interests. The company believes this policy should be effective in increasing shareholder wealth over the medium term.

The board will review its remuneration policy annually to ensure it is effective.

### Performance Income as a proportion of Total Remuneration

Senior executives are paid performance based bonuses based on a proportion of their total remuneration package. The remuneration committee has set these bonuses to encourage achievement of specific goals that have been given a high level of importance in relation to the future growth and financial performance of the Consolidated Entity. The remuneration committee will review the performance bonuses to gauge their effectiveness against achievement of the set goals, and adjust future years' incentives as they see fit, to ensure use of the most cost effective and efficient methods.

All senior executives' remuneration for the year ended 30 June 2010 had a fixed component and a variable component of their overall remuneration, with the variable part of their remuneration paid subject to a performance condition.

### Options Issued as part of remuneration for the year ended 30 June 2010

Options are issued to directors and executives as part of their remuneration. The options are not issued based on performance criteria, but are issued to directors and executives of SomnoMed Limited and its subsidiaries to increase long term goal congruence between executives, directors and shareholders.

Company Directors/ Executives	Granted Number	Grant Date	Value per Option at Grant Date	First Exercise Price	Earliest Exercise Date	Last Exercise Date
Ralf Barschow	260,000	3 September 2009	11.25 cents	58 cents	30 September 2011	30 September 2012
John Truitt	75,000	1 July 2009	12.75 cents	56 cents	1 July 2011	30 June 2012
Chris Bedford	50,000	3 September 2009	11.25 cents	58 cents	30 September 2011	30 September 2012
Neil Verdal-Austin	125,000	15 October 2009	27.69 cents	58 cents	31 October 2011	31 October 2012

### Employment Contracts of Directors and Senior Executives

The employment conditions of the chief executive officer and specified executives are formalised in contracts of employment or its wholly owned subsidiary. All executives are permanent employees of SomnoMed. No contract is for a fixed term. Each contract states it can be terminated by the company by giving up to six months notice and by paying a redundancy of between three to six months.

## DIRECTORS' REPORT (CONTINUED)

### Directors' remuneration

The following table discloses the remuneration of Directors of the company for the year ended 30 June 2010, as specified for disclosure by AASB 124. The information contained in this table is audited.

Director	Short-term Benefits		Post-Employment Benefits	Share-based Payment	Termination Benefits	Total
	Salary & Fees	Other	Superannuation	Options (1)		
Peter Neustadt (2)						
-2009	108,896	-	-	24,750	-	133,646
-2010	108,896	-	-	-	-	108,896
Graham Hurst						
-2009	40,000	-	3,600	9,900	-	53,500
-2010	40,000	-	3,600	-	-	43,600
Paul Hopper (3)						
-2009	40,000	-	-	9,900	-	49,900
-2010	40,000	-	-	-	-	40,000
Alexander Macintosh (resigned 30/06/09)						
-2009	40,000	-	3,600	9,900	-	53,500
-2010	-	-	-	-	-	-
TOTAL 2009	228,896	-	7,200	54,450	-	290,546
TOTAL 2010	188,896	-	3,600	-	-	192,496

- (1) The option amounts disclosed are based on the assessed fair value at the date of grant using the Black-Scholes model and allocated to each reporting period evenly over the period from grant date to vesting date. All options discussed above have vested in the current reporting period on the grant date.
- (2) Dr Neustadt is a director of Belgove Pty Limited, which received consultancy fees during this and the previous year. Belgove Pty Limited was issued with options during the previous year. Refer Note 28 (b) (i) of the accounts for further information.
- (3) Mr Hopper is a director of Kilinwata Investments Pty Limited, which was issued with options during the previous year.
- (4) No Director receives any performance related remuneration.

## DIRECTORS' REPORT (CONTINUED)

### Executives' remuneration

The following table discloses the remuneration of the specified executives of the company and the consolidated entity for the year ended 30 June 2010, as specified for disclosure by AASB 124. The information in this table is audited.

Executive	Short-term Benefits		Post-Employment Benefits	Share-based Payment	Termination Benefits	Total	Percentage of Remuneration Performance Related
	Salary & Fees	Other	Superannuation	Options (1)			
John Truitt							
-2009	230,719	29,090	-	-	-	259,809	10%
-2010	252,225	17,268	-	9,563	-	279,056	9%
Chris Bedford							
-2009	133,945	-	-	12,055	-	146,000	10%
-2010	141,500	-	12,420	5,625	-	159,545	3%
Sergio Herrandiz							
-2009	151,547	-	-	-	-	151,547	5%
-2010	-	-	-	-	-	-	-
Ralf Barschow							
- 2009	300,000	28,947	50,000	51,480	-	430,427	14%
- 2010	336,251	-	25,000	29,250	-	390,501	3%
Neil Verdall-Austin							
- 2009	120,645	-	10,858	14,250	-	145,753	14%
- 2010	189,750	-	16,515	34,612	-	240,877	3%
<b>TOTAL 2009</b>	<b>936,856</b>	<b>58,037</b>	<b>60,858</b>	<b>77,785</b>	<b>-</b>	<b>1,133,536</b>	
<b>TOTAL 2010</b>	<b>919,726</b>	<b>17,268</b>	<b>53,935</b>	<b>79,050</b>	<b>-</b>	<b>1,069,979</b>	

(1) The option amounts disclosed are based on the assessed fair value at the date of grant using the Black-Scholes model and allocated to each reporting period evenly over the period from grant date to vesting date. All options discussed above have vested in the current reporting period on the grant date.

For the year ended 30 June 2010 the Company had four (2009 – five) persons employed who were deemed to be specified executives.

The key management personnel of the consolidated group comprise the directors and the specified executives.

## DIRECTORS' REPORT (CONTINUED)

### Other Information

#### Non-audit Services

The board of directors, in accordance with advice from the audit committee, is satisfied that the provision of non-audit services during the year is compatible with the general standard of independence for auditors imposed by the *Corporations Act 2001*. The directors are satisfied that the services disclosed below did not compromise the external auditor's independence for the following reasons:

- all non-audit services are reviewed and approved by the audit committee prior to commencement to ensure they do not adversely affect the integrity and objectivity of the auditor; and
- the nature of the services provided do not compromise the general principles relating to auditor independence in accordance with APES 110: Code of Ethics for Professional Accountants set by the Accounting Professional and Ethical Standards Board.

Fees of \$16,720 for non-audit services were paid/payable to the external auditors during the year ended 30th June 2010.

#### Auditor's Independence Declaration

The auditor's independence declaration for the year ended 30th June 2010 is set out on page 49 of this annual report.

Signed in accordance with a resolution of the Board of Directors.



.....  
Peter Neustadt

Chairman

24 September 2010

# CORPORATE GOVERNANCE STATEMENT

## Corporate Governance

The Company formally has adopted corporate governance policies and practices as provided by the ASX Listing Rules and the principles of the ASX Corporate Governance Council. The Directors are of the opinion that the Company has complied with the above-mentioned policies. Set out below is more information on the Company's corporate governance policies.

### Board Composition

The skills, experience and expertise relevant to the position of each director who is in office at the date of the annual report and their term of office are detailed in the director's report.

The Board reviews its composition and assesses nominations for new appointments from time to time to ensure the right balance of skills and experience.

The majority of the Board are to be independent directors, having no business or other relationship that could compromise their autonomy.

The Chairman and Chief Executive Officer roles are to be held by different persons.

The Chief Executive Officer may also be a director of the Company. Non-executive directors retire by rotation in accordance with clause 16 of the Constitution.

Newly appointed directors must stand for re-election at the next Annual General Meeting in accordance with clause 16 of the Constitution, with the exception of the Managing Director.

The Board regularly assesses the independence of each non-executive director in the light of interests disclosed by them. The Company does not consider length of tenure as disqualifying criteria for independence.

An independent director is independent of management and free of any business or other relationship that could materially interfere with, or could reasonably be perceived to materially interfere with, the exercise of their unfettered and independent judgement.

In assessing the independence of each director, the board takes into consideration whether the director's shareholding in the Company, relationships with suppliers, customers and competitors, or tenure as a director of the Company would materially affect the director's ability to exercise unfettered and independent judgement in the interests of the Company's shareholders.

Consistent with the emphasis on 'substance over form' advocated by the ASX Guidelines, the Board takes a qualitative approach to materiality, rather than setting strict numerical thresholds, and considers each director's individual circumstances on its merits.

The independence of each director is formally reviewed annually in June each year and at any time when a change occurs that may affect a director's independence. Non-executive directors must formally advise the Chairman of any relevant information, and update the Chairman if their circumstances change at any time.

The names of independent directors of the company are Paul Hopper and Graham Hurst.

Independent directors have the right to seek independent professional advice at the company's expense in the furtherance of their duties as directors. Written approval must be obtained from the chairman prior to incurring any expense on behalf of the company.

The Board has created a number of standing committees:

Audit Committee

Remuneration Committee

### Shareholder Rights

Shareholders are entitled to vote on significant matters impacting on the business, which include the election and remuneration of directors, changes to the Constitution and receipt of annual and interim financial statements. Shareholders are strongly encouraged to attend and participate in the Annual General Meetings of Somnomed Limited, to lodge questions to be responded by the Board and/or the CEO, and are able to appoint proxies.

## CORPORATE GOVERNANCE STATEMENT (CONTINUED)

### Role of the Board

The Company recognises that corporate governance is fundamental to the effective operation of the Company. The Board is the pivotal element of corporate governance, and the Company desires its Board to be effective, independent, representative of stakeholders and valuable to the organisation.

The Board's role is to provide governance of the Company in the best interests of shareholders, having regard to the interests of all stakeholders of the Company. The specific responsibilities of the Board include:

- the overall corporate governance of the Company including its strategic direction, financial objectives, and overseeing (or supervision) of control and accountability systems;
- Input into and approval of strategic plans and goal and performance objectives, key operational and financial matters, as well as major investment and divestment proposals;
- appointing and removing the chief executive officer (or equivalent);
- ratifying the appointment and, where appropriate, the removal of the chief financial officer (or equivalent) and the Company Secretary;
- approving the nominations of Directors to the Board;
- ensuring Management maintains a sound system of internal controls to safeguard the assets of the Group;
- monitoring the performance of the Group;
- reviewing and ratifying systems of risk management and internal compliance and control, codes of conduct, and legal compliance;
- monitoring senior management's performance and implementation of strategy, and ensuring appropriate resources are available;
- approving and monitoring the progress of major capital expenditure, capital management, and acquisitions and divestitures;
- approving and monitoring financial and other Board reporting; and
- the approval of the annual and half yearly financial report.

### Performance Evaluation

An annual self-assessment of the board and all board members is conducted by the board in such manner, as the board deems appropriate.

### Trading Policy

The company's policy regarding directors and employees trading in its securities has been set by the Board. The policy restricts directors and employees from acting on material information until it has been released to the market and adequate time has been given for this to be reflected in the security's prices.

### Audit Committee

The names and qualifications of those appointed to the Audit Committee and their attendance at meetings of the committee are included in the directors' report.

The role of the Audit Committee is to:

- to review proposed reportable financial information and to recommend its approval or otherwise by the Board;
- to review and assess the Company's accounting policies, and determine in consultation with the Chief Financial Officer if any changes to policy should be enacted;
- to communicate with, and monitor the effectiveness of the Company's external auditor; and
- to make recommendations to the Board for the appointment, reappointment or replacement and remuneration of an appropriate independent external auditor.

## CORPORATE GOVERNANCE STATEMENT (CONTINUED)

### Remuneration Committee

The Remuneration Committee comprises the full Board and their attendance at meetings of the committee are detailed in the Directors' Report. The responsibilities of the Remuneration Committee include:

- Assessing the skills and competencies required on the Board, from time to time assessing the extent to which the required skills are represented on the Board;
- Establishing processes for the review of the performance of individual directors and the Board as a whole;
- Encouraging and supporting directors' professional development to enhance director competencies;
- Establishing processes for the identification of suitable candidates for appointment to the Board;
- Developing Board succession plans to maintain an appropriate balance of skills, experience and expertise on the Board;
- Considering recommendations for the appointment and removal of Directors;
- Approving remuneration strategy and policies for senior management and selected packaged employees as well as the individual remuneration arrangements and terms of employment for positions/individuals who are direct reports to the Chief Executive Officer (or similar), ensuring that remuneration policies are not only effective, but that they are also reported and explained to shareholders.

Additional information on the Company's remuneration principles is contained in the Remuneration Report contained in the Directors' Report.

### Continuous Disclosure and ASX Announcements

- Directors and Executive Management are to be aware of the continuous disclosure regulations in the ASX Listing Rules.
- In the event that any Director or member of management becomes aware of any fact or circumstance which may give rise to a requirement to disclose such information under the Listing Rules, they are required to immediately inform either the Company Secretary, the CEO (or similar), the CFO or the Chairman.
- Prior to disclosure, the CFO will review the information to enable a judgement as to the appropriate disclosure, if any, to be made.
- If there is uncertainty over the requirement to comply with the continuous disclosure requirements, then the Company will seek external legal advice. The Company, through the Company Secretary, will notify the ASX of any information it is determined is required to be disclosed.

Where announcements are made to the market through the ASX, such announcements are pre-vetted by the CFO, Chairman and Board of Directors to ensure that such statements are:

- factual;
- do not omit material information; and
- are expressed in a clear and objective manner.

### Corporate Reporting

The Company strives to convey to its shareholders and the investing public pertinent information in a detailed, regular, factual and timely manner. Information is communicated to shareholders through: the Annual Financial Report, disclosures to the ASX, notices and explanatory memoranda of Annual General Meetings; and SomnoMed's website at [www.somnomed.com.au](http://www.somnomed.com.au).

### Risk Management

The board is committed to the Senior executives and management are expected to practise sensible risk management in the day-to-day performance of their duties and are required to escalate any material issues, which arise or have the potential to arise. The CEO has the primary responsibility to advise the Board of material risk items, which arise and together the Board and senior management are responsible for taking all reasonable steps to address and mitigate such risk items.

**SOMNOMED LIMITED**  
ACN 003255221  
**CONSOLIDATED INCOME STATEMENT**  
**FOR THE YEAR ENDED 30 JUNE 2010**

	Note	2010 \$	2009 \$
Sales revenue	5	10,714,174	7,737,777
Cost of sales		(4,630,002)	(3,678,614)
<b>Gross margin</b>		<b>6,084,172</b>	<b>4,059,163</b>
Sales and marketing expenses		(2,455,327)	(2,597,795)
Administrative expenses		(1,785,918)	(1,442,837)
<b>Operating profit/(loss) before corporate and business development expenses, non cash items and income tax</b>		<b>1,842,927</b>	<b>18,531</b>
Corporate and business development expenses		(1,768,795)	(1,786,402)
Other revenue and grants	5	188,437	257,697
Revenue from investment activities		89,389	228,096
Share and options expense	25c	(87,877)	(139,980)
Depreciation and amortization		(156,396)	(318,781)
Loss on transfer of intellectual property		-	(53,064)
Share of profit/(loss) of associated company		29,098	(8,977)
Unrealised foreign exchange loss		(76,509)	-
Unrealised gain on derivatives		54,174	-
<b>Operating profit/(loss) before income tax</b>	6	<b>114,448</b>	<b>(1,802,880)</b>
Income tax (expense)/benefit attributable to operating profit/(loss)	7	671,695	(15,793)
<b>Operating profit/(loss) attributable to members of the parent entity</b>		<b>786,143</b>	<b>(1,818,673)</b>
Basic earnings per share (cents)	23	2.0	(4.7)
Diluted earnings per share (cents)	23	2.0	(4.7)

The accompanying notes form part of these financial statements.

**CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME  
FOR THE YEAR ENDED 30 JUNE 2010**

	2010	2009
	\$	\$
Profit/(loss) for the period	786,143	(1,818,673)
Other comprehensive income:		
Foreign exchange translation difference for foreign operations	7,371	3,263
Other comprehensive income for the period	7,371	3,263
Total comprehensive income attributable to members of the parent entity	<b>793,514</b>	<b>(1,815,410)</b>

The accompanying notes form part of these financial statements.

**CONSOLIDATED BALANCE SHEET  
AS AT 30 JUNE 2010**

	Note	2010 \$	2009 \$
<b>CURRENT ASSETS</b>			
Cash and cash equivalents	8	4,293,676	4,008,934
Trade and other receivables	9	1,583,519	1,426,190
Inventory	10	197,220	83,756
<b>TOTAL CURRENT ASSETS</b>		<b>6,074,415</b>	<b>5,518,880</b>
<b>NON-CURRENT ASSETS</b>			
Property, plant and equipment	12	641,924	235,490
Intangible assets	13	231,674	283,634
Investment in associate entity	11	29,098	-
Deferred tax asset	7d	856,701	-
<b>TOTAL NON-CURRENT ASSETS</b>		<b>1,759,397</b>	<b>519,124</b>
<b>TOTAL ASSETS</b>		<b>7,833,812</b>	<b>6,038,004</b>
<b>CURRENT LIABILITIES</b>			
Trade and other payables	14	1,872,625	1,455,862
Provisions	15	308,834	248,896
<b>TOTAL CURRENT LIABILITIES</b>		<b>2,181,459</b>	<b>1,704,758</b>
<b>NON CURRENT LIABILITIES</b>			
Trade and other payables	14	1,715	-
<b>TOTAL LIABILITIES</b>		<b>2,183,174</b>	<b>1,704,758</b>
<b>NET ASSETS</b>		<b>5,650,638</b>	<b>4,333,246</b>
<b>SHAREHOLDERS' EQUITY</b>			
Issued capital	16	23,706,829	23,270,829
Reserves	17	1,334,268	1,239,020
Accumulated losses		(19,390,459)	(20,176,603)
<b>TOTAL EQUITY</b>		<b>5,650,638</b>	<b>4,333,246</b>

The accompanying notes form part of these financial statements.

**CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY  
FOR THE YEAR ENDED 30 JUNE 2010**

	Issued Capital	Share Option Reserve	Foreign Currency Translation Reserve	Accumulated Losses	Total
	\$	\$	\$	\$	\$
Balance at 1 July 2008	23,270,829	1,146,939	(51,162)	(18,357,930)	6,008,676
Share option reserve on recognition of remuneration options	-	139,980	-	-	139,980
Total other comprehensive income	-	-	3,263	-	3,263
Profit/(loss) attributable to members of parent entity	-	-	-	(1,818,673)	(1,818,673)
Balance at 30 June 2009	23,270,829	1,286,919	(47,899)	(20,176,603)	4,333,246
Shares issued during the year	436,000	-	-	-	436,000
Share option reserve on recognition of remuneration options	-	87,877	-	-	87,877
Total other comprehensive income	-	-	7,371	-	7,371
Profit/(loss) attributable to members of parent entity	-	-	-	786,144	786,144
Balance at 30 June 2010	23,706,829	1,374,796	(40,528)	(19,390,459)	5,650,638

The accompanying notes form part of these financial statements.

**CONSOLIDATED CASH FLOW STATEMENT  
FOR THE YEAR ENDED 30 JUNE 2010**

	Note	2010 \$	2009 \$
<b>Cash flows from operating activities</b>			
Receipts from customers		10,578,187	7,402,424
Grants received		80,713	332,697
Payments to suppliers and employees		(10,286,826)	(9,276,477)
Interest received		89,389	223,933
Net cash inflow/(outflow) from operating activities	22	461,463	(1,317,423)
<b>Cash flows from investing/financing activities</b>			
Payments to associated company		-	(193)
Proceeds from issue of shares		436,000	-
Payments for intellectual property		-	(53,064)
Payments for investments		-	(8,977)
Payments for property, plant and equipment		(526,815)	(43,941)
Net cash inflow/(outflow) from investing/financing activities		(90,815)	(106,175)
Net increase/(decrease) in cash held		370,648	(1,423,598)
Cash at beginning of the financial year		4,008,934	5,432,532
Exchange rate adjustment		(85,906)	-
Cash at the end of the financial year	21	4,293,676	4,008,934

The accompanying notes form part of these financial statements.

# NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2010

## 1. REPORTING ENTITY

SomnoMed Limited is a company domiciled in Australia. The consolidated financial statements of the Company as at and for the year ended 30 June 2010 comprise the Company and its controlled entities (together referred to as the Consolidated Entity). The Consolidated Entity produces and sells devices for the oral treatment of sleep related disorders.

## 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) (including Australian Interpretations) adopted by the Australian Accounting Standards Board and the Corporations Act 2001. The financial report of the Consolidated Entity and the financial report of the Company comply with International Financial Reporting Standards and Interpretations adopted by the International Accounting Standards Board.

### b. Basis of measurement

The consolidated financial statements have been prepared on the historical cost basis.

### c. Functional and presentation currency

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

### d. Use of judgments and estimates

The preparation of financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and 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 period in which the estimate is revised and in any future periods affected.

## 3. SIGNIFICANT ACCOUNTING POLICIES

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements and have been applied consistently by all entities in the Consolidated Entity.

### a. Basis of Consolidation

#### *Controlled entities*

Controlled entities are entities controlled by the Company. Control exists when the Company has power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that presently are exercisable or convertible are taken into account. 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. Investments in controlled entities are carried at their cost of acquisition in the Company's financial statements.

#### *Transactions eliminated on consolidation*

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

### b. Income Recognition

Revenues are recognised at fair value of the consideration received net of the amount of goods and services tax (GST).

#### *Sales revenue*

Sales revenue comprises revenue earned (net of returns, discounts and allowances) from the provision of products. Revenue from the sale of goods is recognised upon dispatch of goods to customers.

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2010

### *Other income*

Other income, including government grants, is recognised on a systematic basis over the periods necessary to match it with the related costs for which it is intended to compensate or, if the costs have already been incurred, in the period in which it becomes receivable. The income is deemed to be receivable when the entitlement is confirmed. Dividend income from subsidiaries is recognised by the parent when the dividends are declared by the subsidiary.

### **c. Goods and Services Tax**

Revenues, expenses and assets are recognised net of the amount of GST, except where the amount of GST incurred is not recoverable from the taxation authority. In these circumstances, 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.

### **d. Foreign Currency**

#### *Foreign currency transactions*

Transactions in foreign currencies are translated to the respective functional currencies of controlled 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 transactions 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, including goodwill and fair value adjustments arising on acquisition, generally are translated to the functional currency at foreign exchange rates ruling at the reporting date. The revenues and expenses of foreign operations are translated to the functional currency at rates approximating the foreign exchange rates ruling at the dates of transactions. Foreign currency differences arising from translation of controlled entities with a different functional currency to that of the Consolidated Entity are recognised in the foreign currency translation reserve (FCTR). When a foreign operation is disposed of, in part or in full, the relevant amount of its FCTR is transferred to profit or loss.

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 directly in equity in the FCTR.

### **e. Cash and cash equivalents**

Cash and cash equivalents comprise cash balances and call deposits with an original maturity of three months or less.

### **f. Financial Instruments**

#### *Derivative Financial Instruments*

The Consolidated Entity holds derivative financial instruments to hedge its exposure to foreign exchange risk arising from operating, investing and financing activities. In accordance with its treasury policy, The Consolidated Entity does not hold or issue derivative financial instruments for trading purposes. However, derivatives are not hedge accounted and are accounted for as trading instruments.

Derivative financial instruments are recognised initially at fair value. Attributable transaction costs are recognised in the income statement when incurred. Subsequent to initial recognition, derivative financial instruments are measured at fair value with changes in fair value accounted for as described below.

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2010

### *Non-derivative financial assets and liabilities*

Non-derivative financial instruments comprise investments in equity, trade and other receivables, cash and cash equivalents, loans, and trade and other payables.

Non-derivative financial instruments are recognised initially at fair value plus, for instruments not at fair value through the income statement, any attributable transaction costs. Subsequent to initial recognition, non-derivative financial instruments are measured as described below.

Accounting for finance income is discussed in accounting policy (o).

### *Determination of fair values*

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 a risk free interest rate based upon government bonds.

### *Other*

Other non-derivative financial instruments are measured at amortised cost using the effective interest rate method, less any impairment losses.

## **g. Provisions**

A provision is recognised in the balance sheet when the Consolidated Entity has a present legal or constructive obligation as a result of a past event that can be measured reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation.

### *Warranties*

Provisions for warranty claims are made for claims in relation to sales made prior to the reporting date, based on historical claim rates and respective product populations. The provision is determined on a discounted cash flow basis. Warranty periods on MAS devices are for up to two years.

### *Make good lease costs*

The Consolidated Entity has an operating lease over its premises that require the premises to be returned to the lessor in its original condition. The operating lease payments do not include an element for the repairs/overhauls. A provision for make good lease costs is recognised at the time it is determined that it is probable that such costs will be incurred in a future period, measured at the expected cost of returning the asset to the lessor in its original condition. An offsetting asset of the same value is also recognised and is classified in property, plant and equipment. This asset is amortised to the income statement over the life of the lease.

### *Research and development expenditure*

Research and Development costs are charged to profit/(loss) before income tax as incurred.

### *Other intangible assets*

Intellectual property, acquired is stated at cost less accumulated amortisation (see below) and impairment losses (see accounting policy (h)).

### *Subsequent expenditure*

Subsequent expenditure on capitalised intangible assets is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is expensed as incurred.

### *Amortisation*

Amortisation is recognised in the income statement on a straight-line basis over the estimated useful lives of the intangible assets from the date they are available for use unless such lives are indefinite. Intangible assets with an indefinite useful life are systematically tested for impairment annually. The estimated useful lives for the current and comparative periods are as follows:

Patents- 10 years

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2010

### **h. Impairment**

The carrying amounts of the Consolidated Entity's assets, other than inventories (see accounting policy (j)) are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated (see below). An impairment loss is recognised whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. Impairment losses are recognised in the income statement unless the asset has previously been revalued, in which case the impairment loss is recognised as a reversal to the extent of that previous revaluation with any excess recognised through the income statement. Impairment losses recognised in respect of cash generating units are allocated first to reduce the carrying amount of any goodwill allocated to the cash generating unit or a group of units and then, to reduce the carrying amount of the other assets in the unit or a group of units on a pro-rata basis.

#### *Calculation of recoverable amount*

##### **Receivables**

The recoverable amount of the Consolidated Entity's investments in receivables carried at amortised cost is calculated as the present value of estimated future cash flows, discounted at the original effective interest rate (i.e. the effective interest rate computed at initial recognition of these financial assets). Receivables with a short duration are not discounted. Impairment of receivables is not recognised until objective evidence is available that a loss event has occurred. Significant receivables are individually assessed for impairment. Impairment testing of significant receivables that are not assessed as impaired individually is performed by placing them into portfolios of significant receivables with similar risk profiles and undertaking a collective assessment of impairment. Non-significant receivables are not individually assessed. Instead, impairment testing is performed by placing non-significant receivables in portfolios of similar risk profiles, based on objective evidence from historical experience adjusted for any effects of conditions existing at each balance date. The allowance for impairment is calculated with reference to the profile of debtors in the Consolidated Entity's sales and marketing regions.

##### *Other Assets*

The recoverable amount of other assets is the greater of their fair value less costs to sell, and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For the purpose of impairment testing, assets are grouped together into the smallest group of assets that generate cash flows from continuing use that are largely independent of the cash flows of other assets or groups of assets (cash generating units). The goodwill acquired in a business combination, for the purpose of impairment testing is allocated to the cash generating units that are expected to benefit from the synergies of the combination. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

##### *Reversals of Impairment*

An impairment loss in respect of a receivable carried at amortised cost is reversed if the subsequent increase in recoverable amount can be related objectively to an event occurring after the impairment loss was recognised. An impairment loss in respect of goodwill is not reversed. In respect of other assets, an impairment loss is reversed when there is an indication that the impairment loss may no longer exist and 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.

### **i. Property, Plant and Equipment**

#### *Owned assets*

Items of property, plant and equipment are stated at cost less accumulated depreciation (see below) and impairment losses (see accounting policy (h)). An asset's cost is determined as the consideration provided plus incidental costs directly attributable to the acquisition. Subsequent costs in relation to replacing a part of property, plant and equipment are recognised in the carrying amount of the item if it is probable that future economic benefits embodied within the part will flow to the Consolidated Entity and its cost can be measured reliably. All other costs are recognised in the income statement as incurred.

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2010

### *Leased assets - Operating leases*

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 recognised in the income statement on a straight-line basis. Items of property, plant and equipment, including leasehold assets, are depreciated using the straight-line method over their estimated useful lives, taking into account estimated residual values. Assets are depreciated 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 periods only.

The estimated useful lives in the current and comparative periods are as follows:

Leasehold improvements	1 – 3 years
Plant & equipment	3 – 20 years

### **j. Inventories**

Inventories are measured at the lower of cost and net realisable value. 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. Cost is based on the first-in-first-out principle and includes expenditure incurred in acquiring the inventories and bringing them to their existing condition and location.

### **k. Employee Benefits**

#### *Wages, salaries and annual leave*

Liabilities for employee benefits for wages, salaries and annual leave expected to settle within 12 months of the year end represent present obligations resulting from employees' services provided up to reporting date, calculated at undiscounted amounts based on remuneration wage and salary rates that the Consolidated Entity expects to pay as at reporting date including related on-costs, such as workers' compensation insurance and payroll tax.

#### *Share based payments*

The Company has granted options to certain directors and employees. The fair value of options and shares granted is recognised as a share and option expense with a corresponding increase in equity. The fair value is measured at the date the options or shares are granted taking into account market based criteria and expensed over the vesting period after which the employees become unconditionally entitled to the options and shares. The fair value of the options granted is measured using the Black-Scholes method, taking into account the terms and conditions attached to the options. The fair value of the performance shares granted is measured using the weighted average share price of ordinary shares in the Company, taking into account the terms and conditions attached to the shares. The amount recognised as an expense is adjusted to reflect the actual number of options and shares that vest except where forfeiture is due to market related conditions.

### **l. Receivables**

Trade and other receivables are stated at amortised cost less impairment losses (see accounting policy (h)).

### **m. Taxation**

Income tax expense in the income statement for the periods presented comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity. Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantially enacted at reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is calculated using the balance sheet method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Temporary differences are not provided for the initial recognition of goodwill and other assets or liabilities in a transaction that affects neither accounting nor taxable profit, or differences relating to investments in subsidiaries to the extent that it is probable that they will not reverse in the foreseeable future.

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2010

Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based upon the laws that have been enacted at reporting date. A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reviewed at each reporting date and reduced to the extent that it is no longer probable that the related tax benefit will be realised. Additional income taxes that arise from the distribution of dividends are recognised at the same time as the liability to pay the related dividend is recognised.

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they relate to income taxes levied by the same tax authority on the same taxable entity or on a different tax entity but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realised simultaneously.

### **n. Payables**

Trade and other payables are stated at amortised cost.

### **o. Finance income and expense**

Interest income is recognised as it accrues in the income statement using the effective interest method.

### **p. Earnings per share**

The Consolidated Entity presents basic and diluted earnings per share (EPS) for its ordinary shares. Basic EPS is calculated by dividing the net profit/(loss) attributable to equity holders of the parent for the financial period, after excluding any costs of servicing equity (other than ordinary shares) by the weighted average number of ordinary shares of the Company, adjusted for any bonus issue.

Diluted EPS is calculated using the basic EPS earnings as the numerator. The weighted average number of shares used as the denominator is adjusted by the after-tax effect of financing costs associated with the dilutive potential ordinary shares and the effect on revenues and expenses of conversion to ordinary shares associated with dilutive potential ordinary shares adjusted for any bonus issue.

### **q. Segment Reporting - Determination and presentation of operating segments**

As of 1 July 2009, The Consolidated Entity determines and presents operating segments based on the information that internally is provided to the Board of Directors, who are The Consolidated Entity's chief operating decision maker. This change in accounting policy is due to the adoption of IFRS 8 Operating Segments. Previously, operating segments were determined and presented in accordance with AASB 114 Segment Reporting. The new accounting policy in respect of segment operating disclosures is presented as follows:

Comparative segment information has been re-presented in conformity with the transitional requirements of IFRS 8. Since the change in accounting policy only impacts presentation and disclosure aspects, there is no impact on net profit or EPS.

An operating segment is a component of The Consolidated Entity that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to transactions with any of The Consolidated Entity's other components if separately reported and monitored. An operating segment's operating results are reviewed regularly by the Board of Directors to make decisions about resources to be allocated to the segment and assess its performance, and for which discrete financial information is available.

Segment results that are reported to the Board of Directors include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Unallocated items comprise mainly corporate head office results.

### **r. Accounting judgment and estimates**

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

#### *Key sources of estimation uncertainty*

In particular, information about significant areas of estimation, uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amounts recognised in the financial statements is described in the following areas:

- Intangible assets, Provisions, Employee benefits and Financial instruments

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2010

### s. Share Capital

#### *Ordinary shares*

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

### t. Presentation of Financial Statements

The Consolidated Entity applies revised AASB 101 Presentation of Financial Statements (2007), which became effective as of 1 January 2009. As a result, The Consolidated Entity presents in the statement of changes in equity all owner changes in equity, whereas all non-owner changes in equity are presented in the statement of comprehensive income. This presentation has been applied in this Financial Report at and for the year ended 30 June 2010.

### u. New standards and interpretations not yet adopted

The following standards, amendments to standards, and interpretations have been identified as those which may impact the entity in the period of initial application. They are available for early adoption at 30 June 2010, but have not been applied in preparing this Financial Report:

AASB 9 Financial Instruments;

AASB 124 Related Party Disclosures;

AASB 2009-5 Further Amendments to Australian Accounting Standards arising from the Annual Improvements Project;

AASB 2009-8 Amendments to Australian Accounting Standards - Group Cash-settled Share-based Payment Transactions;

AASB 2009-10 Amendments to Australian Accounting Standards - Classification of Rights Issues;

AASB 2009-14 Amendments to Australian Interpretation - Prepayments of a Minimum Funding Requirement; and

IFRIC 19 Extinguishing Financial Liabilities with Equity Instruments.

The impact of these standards and interpretations is not considered to be significant and will be applied by The Consolidated Entity on the relevant application date.

## 4. FINANCIAL RISK MANAGEMENT

### Overview

The Company and Consolidated Entity have exposure to the following risks from the use of financial instruments:

- Credit risk
- Liquidity risk
- Market risk

This note presents information about the Company's and the Consolidated Entity's exposure to each of the above risks, their objectives, policies and processes for measuring and managing risk, and the management of capital. Further quantitative disclosures are included throughout these consolidated financial statements. The Board of directors has overall responsibility for the establishment and oversight of the risk management and monitors operational and financial risk management throughout the Consolidated Entity. Monitoring risk management includes ensuring appropriate policies and procedures are published and adhered to. The Management reports to the Audit Committee.

The Board aims to manage the impact of short-term fluctuations on the Company's and the Consolidated Entity's earnings. Over the longer term, permanent changes in market rates will have an impact on earnings.

The Company and the Consolidated Entity are exposed to risks from movements in exchange rates and interest rates that affect revenues, expenses, assets, liabilities and forecast transactions. Financial risk management aims to limit these market risks through ongoing operational and finance activities.

Exposure to credit, foreign exchange and interest rate risks arises in the normal course of the Company's and the Consolidated Entity's business. Derivative financial instruments are not used to hedge exposure to fluctuations in foreign exchange rates.

The Audit Committee oversees adequacy of the company's risk management framework in relation to the risks faced by the Company and the Consolidated Entity.

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2010

### **Credit Risk**

Credit risk is the risk of financial loss to the Company or the Consolidated Entity if a customer, controlled entity or counterparty to a financial instrument fails to meet its contractual obligations and arises principally from the Company's and the Consolidated Entity's receivables from customers.

#### *Trade and other receivables*

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

Policies and procedures of credit management and administration of receivables are established and executed at a regional level. Individual regions deliver reports to management and the Board on debtor ageing and collection activities on a monthly basis.

In monitoring customer credit risk, the ageing profile of total receivables balances is reviewed by management by geographic region on a monthly basis. Regional management is responsible for identifying high risk customers and placing restrictions on future trading, including suspending future shipments and administering dispatches on a prepayment basis.

The Company and the Consolidated Entity have established an allowance for impairment that represents their estimate of incurred losses in respect of trade and other receivables.

### **Liquidity Risk**

Liquidity risk is the risk that the Consolidated Entity will not be able to meet its financial obligations as they fall due. The Consolidated Entity's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Consolidated Entity's reputation.

The Consolidated Entity monitors cash flow requirements and produces cash flow projections for the short and long term with a view to optimising return on investments. Typically, the Consolidated Entity ensures that it has sufficient cash on demand to meet expected operational net cash flows for a period of at least 30 days, including the servicing of financial obligations. This excludes the potential impact of extreme circumstances that cannot reasonably be predicted, such as natural disasters.

### **Market Risk**

Market risk is the risk that changes in market prices such as foreign exchange rates, interest rates and equity prices will affect the Company's and the Consolidated Entity's net loss or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return.

#### *Currency Risk*

The Consolidated Entity is exposed to currency risk on sales and purchases that are denominated in a currency other than the respective functional currencies of the controlled entities, primarily Australian dollars (AUD), but also United States dollars (USD), Euros (EUR), Swiss francs (CHF), Singapore dollar (SGD) and Philippines Pesos (PHP). The currencies in which these transactions primarily are denominated are AUD, USD, EUR, CHF, SGD and PHP.

Over 80%(2009:75%) of the Consolidated Entity's revenues and over 70%(2009:60%) of costs are denominated in currencies other than AUD. Risk resulting from the translation of assets and liabilities of foreign operations into the Consolidated Entity's reporting currency is not hedged.

#### *Interest Rate Risk*

The Consolidated Entity is exposed to interest rate risks in Australia. See note 30 for effective interest rates.

### **Capital Management**

The Consolidated Entity's objectives when managing capital are to safeguard its ability to continue as a going concern, to provide returns to shareholders, to provide benefits to other stakeholders and to maintain an optimal capital structure to reduce the cost of capital. The Board aims to maintain and develop a capital base appropriate to the Consolidated Entity. In order to maintain or adjust the capital structure, the Consolidated Entity can issue new shares. The Board of directors undertakes periodic reviews of the Consolidated Entity's capital management position to assess whether the capital management structure is appropriate to meet the Consolidated Entity's medium and long-term strategic requirements. Neither the Company nor any of its subsidiaries is subject to externally imposed capital requirements. There were no significant changes in the approach to capital management during the year.

**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 30 JUNE 2010**

	2010	2009
	\$	\$
<b>5. REVENUE</b>		
<b>Operating activities</b>		
Other revenue and grants	188,437	257,697
Interest received - other persons	89,389	228,096
Revenue from sale of goods, net of discounts	10,714,174	7,737,777
	10,992,000	8,223,570

**6. PROFIT/(LOSS) FOR THE YEAR**

Profit/(loss) for the year is after charging:

Operating lease rentals	308,394	293,581
Profit on disposal of property, plant and equipment	-	1,137
Employee benefits expense	3,342,613	3,435,592
Depreciation	104,436	266,821
Amortisation of intellectual property	51,960	51,960

**7. INCOME TAX EXPENSE**

a. The components of tax expense comprise:

Current tax	(150,297)	(15,793)
Deferred tax	821,992	-
	671,695	(15,793)

b. The prima facie tax on profit/(loss) before income tax is reconciled to the income tax expense as follows:

Prima facie income tax expense calculated at 30% of profit/(loss) using the company's domestic tax rate	34,334	(545,602)
Increase/(decrease) in income tax expense due to non-deductible/(assessable) items	10,353	(95,705)
Deferred tax asset due to tax losses and temporary differences not recognised	627,008	641,307
Income tax expense	671,695	(15,793)

c. Deferred tax assets not brought to account

Deferred tax assets not brought to account, the benefits of which will only be realised if the conditions for deductibility set out in Note 3(m) occur

Tax losses	3,482,754	3,984,726
Temporary differences	980,913	1,062,757
	4,463,667	5,047,483

**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 30 JUNE 2010**

**7. INCOME TAXES (Continued)**

	Note	2010 \$	2009 \$
<b>d. Deferred tax assets</b>			
<b>Recognised deferred tax assets</b>			
Property, plant and equipment		9,517	-
Accruals		28,504	-
Provisions		15,379	-
Tax loss carry-forwards		768,592	-
		821,992	-
FX Adjustment		34,719	-
<b>Deferred tax assets</b>		<b>856,701</b>	<b>-</b>

**Movement in temporary differences during the year**

Carrying amount at beginning of financial year		-	-
Recognised in the income statement	7a	821,992	-
<b>Carrying amount at end of financial year</b>		<b>821,992</b>	<b>-</b>

**8. CASH AND CASH EQUIVALENTS**

Cash at bank and on deposit and money market securities		4,293,676	4,008,934
		4,293,676	4,008,934

**9. TRADE AND OTHER RECEIVABLES (Current)**

Trade Debtors		1,371,489	1,251,754
Less provision for doubtful debts		(75,534)	(71,264)
		1,295,955	1,180,490
Prepaid seminar expenses		-	181,641
Other debtors		233,204	63,866
Forward exchange contracts		54,174	-
Loan to associated company		186	193
		1,583,519	1,426,190

All amounts are not interest bearing and are normally settled within 60 days.

**10. INVENTORY**

Inventory		197,220	83,756
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**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 30 JUNE 2010**

**11. INVESTMENT IN ASSOCIATED COMPANY**

Interests are held in the following associated company

Name	Principal Activities	Country of Incorporation	Ownership Interest		Carrying amount of Investment (note11(a))	
			2010	2009	2010	2009
			%	%	\$	\$
SMH Biomaterial AG	Material manufacturer	Switzerland	50	50	29,098	-

2010	2009
\$	\$

**a. Movements During the Year in Equity Accounted Investment in Associated Company**

Balance at beginning of the financial year		-	-
Add new investments during the year		-	8,977
Share of associated company's profit/(loss) after income tax	11b	29,098	(8,977)
Balance at end of the financial year		<u>29,098</u>	<u>-</u>

**b. Equity accounted profit/(loss) of associate is broken down as follows:**

Share of associate's profit/(loss) before income tax expense	53,453	(30,794)
Share of associate's profit/(loss) not recognised	(24,318)	21,867
Share of associate's income tax expense	(37)	(50)
Share of associate's profit/(loss) after income tax	<u>29,098</u>	<u>(8,977)</u>

**c. Summarised Presentation of Aggregate Assets, Liabilities and Performance of Associated Company**

Current assets	195,600	115,201
Non-current assets	2	2
Total assets	<u>195,602</u>	<u>115,203</u>
Current liabilities	22,615	43,529
Non-current liabilities	19,976	23,930
Total liabilities	<u>42,591</u>	<u>67,459</u>
Net assets	153,011	47,744
Revenues	266,537	86,947
Profit/(Loss) after income tax of associated company	106,863	(61,687)

**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 30 JUNE 2010**

**12. PROPERTY, PLANT AND EQUIPMENT**

Plant and equipment -at cost	1,794,210	1,267,395
Accumulated depreciation	(1,152,286)	(1,031,905)
	641,924	235,490

Movements in the carrying amounts of plant and equipment during the current financial year:

Balance at the beginning of the year	235,490	457,232
Additions	526,815	43,491
Disposals	-	(2,859)
Depreciation expense	(104,436)	(266,821)
Effect of movements in foreign exchange	(15,945)	4,447
Carrying amount at the end of the year	641,924	235,490

**13. INTANGIBLE ASSETS**

Patents and trademarks – at cost	519,620	519,620
Accumulated amortisation	(287,946)	(235,986)
	231,674	283,634

**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 30 JUNE 2010**

	2010 \$	2009 \$
<b>14. TRADE AND OTHER PAYABLES</b>		
CURRENT		
Trade creditors and accruals	1,696,777	1,259,492
Income received in advance	175,848	196,370
	1,872,625	1,455,862

All amounts are not interest bearing and are normally settled on 45 day terms

NON CURRENT

Other creditors	1,715	-

**15. PROVISIONS**

Warranty	78,035	54,221
Lease make good	67,212	67,212
Employee entitlements	163,587	127,463
	308,834	248,896

**16. ISSUED CAPITAL**

Issued and fully paid ordinary shares		
39,432,756 (2009-38,382,638) ordinary shares *	23,706,829	23,270,829
Balance at the beginning of year	23,270,829	23,270,829
Shares issued during period:		
- 400,000 pursuant to exercise of options at 40 cents on 24 June 2010	160,000	-
- 50,000 pursuant to exercise of options at 72 cents on 22 April 2010	36,000	-
- 300,000 pursuant to exercise of options at 40 cents on 22 April 2010	120,000	-
- 300,000 pursuant to exercise of options at 40 cents on 27 May 2010	120,000	-
	23,706,829	23,270,829

\* On 26 November 2009, the company's shares were consolidated, with one new share being issued for each existing twenty shares on issue at that date. The number of shares shown in the above table reflects the number of post consolidation shares (including comparatives). An additional 118 shares were issued as a result of the rounding of holdings on consolidation of the shares.

Ordinary shares participate in dividends and the proceeds on winding up of the Company in proportion to the number of shares held.

At shareholders' meetings each ordinary share is entitled to one vote when a poll is called, otherwise each shareholder has one vote on a show of hands.

At 30 June 2010 there were 2,257,500 (2009: 2,805,000) unissued ordinary shares for which options were outstanding.

Subsequent to 30 June 2010 a further 370,000 options were issued to executives and staff.

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2010

	2010 \$	2009 \$
<b>17. RESERVES</b>		
Share option reserve	1,374,796	1,286,919
Foreign currency translation reserve	(40,528)	(47,899)
	1,334,268	1,239,020

The share option reserve records items recognised as expenses on valuation of share option issues as remuneration.

### 18. REMUNERATION OF AUDITORS

Remuneration of the Company's auditors for:

Auditing or reviewing the financial report	38,000	34,500
Other services	16,720	6,883
Remuneration of the Company's other auditors for auditing or reviewing the financial reports of subsidiaries	53,754	28,314
Total auditors' remuneration included in operating result	108,474	69,697

### 19. SEGMENT OPERATIONS

#### Primary Reporting – Business Segments

The Consolidated Entity produces and sells devices for the oral treatment of sleep related disorders, which is the only business segment.

#### Secondary Reporting – Geographical Segments

Geographic location:	Asia Pacific	USA	Europe	Eliminations	Total
<b>2010</b>	\$	\$	\$	\$	\$
External sales revenue	1,874,107	7,475,417	1,364,650	-	10,714,174
Segment net profit/(loss) before tax	183,687	1,960,241	(134,863)	-	2,009,065
Unallocated expense items					(1,984,006)
Interest received					89,389
Profit before tax					114,448
Income tax benefit					671,695
Profit after tax					786,143

Geographic location:	Asia Pacific	USA	Europe	Eliminations	Total
<b>2009</b>	\$	\$	\$	\$	\$
External sales revenue	1,518,798	5,617,826	601,153	-	7,737,777
Segment net profit/(loss) before tax	(381,885)	612,129	(667,150)	-	(436,906)
Unallocated items					(1,594,070)
Interest Received					228,096
Loss before tax					(1,802,880)
Income tax expense					(15,793)
Loss after tax					(1,818,673)

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2010

### 20. PARTICULARS RELATING TO CONTROLLED AND ASSOCIATED ENTITIES

(a) Details of controlled entities are reflected below

Company	Country of Incorporation	Interest %	
		2010	2009
SomnoMed Limited	Australia	-	-
<b>Entities controlled by SomnoMed Limited</b>			
SomCentre Pty Limited (formerly Amelia Blue Pty Limited)	Australia	100%	100%
SomnoMed Inc.	USA	100%	100%
SomnoDent Pty Limited	Australia	100%	100%
SomnoMed Pte Ltd	Singapore	100%	100%
SomnoMed AG	Switzerland	100%	100%
SomnoMed Corporation Japan	Japan	100%	100%
SomnoMed Nordic AB	Sweden	100%	-
SomnoMed Philippines Inc.	Philippines	100%	-
<b>(b) Details of associated entity</b>			
Associated entity of SomnoMed Limited			
SMH Biomaterial AG	Switzerland	50%	50%

### 21. RECONCILIATION OF CASH

	2010	2009
	\$	\$
Cash at the end of the financial year as shown in the cash flow statement is reconciled to the related items in the balance sheet as follows:		
Cash at bank and on deposit and money market securities	4,293,676	4,008,934
	4,293,676	4,008,934

### 22. RECONCILIATION OF OPERATING PROFIT/(LOSS) AFTER INCOME TAX TO NET CASH INFLOW/(OUTFLOW) FROM OPERATING ACTIVITIES

Operating Profit/(Loss) after income tax	786,144	(1,818,673)
Share and Option expense	87,877	139,980
(Profit)/Loss from sale of fixed asset	-	(1,137)
Loss on transfer of intellectual property	-	53,064
Share of associate company loss/(profit)	(29,098)	8,977
Net exchange differences	76,509	3,264
Depreciation and amortization	156,396	318,781
<b>Change in operating assets and liabilities</b>		
(Increase)/Decrease in inventories	(113,463)	(50,784)
(Increase)/Decrease in receivables	(157,330)	(679,922)
Increase/(Decrease) in other payables	412,165	620,778
Increase/(Decrease) in provisions	59,938	88,249
(Increase) in deferred tax assets	(823,991)	-
Increase in lease liability	6,316	-
Net Cash inflow/(outflow) from operating activities	461,463	(1,317,423)

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2010

### 23. EARNINGS PER SHARE

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

	2010	2009
Net profit/ (loss) used in calculating basic and diluted earnings per share	\$786,143	(\$1,818,673)
Basic and diluted profit/(loss) per share (cents per share)	2.0	(4.7)
Weighted average number of shares used in the calculation of diluted earnings per share	38,980,020	38,382,638
Weighted average number of shares used in the calculation of basic earnings per share	38,483,411	38,382,638
Shares on issue at year end	39,432,756	38,382,638
Number of options on issue at year end – each option is exercisable at between 20 cents and 80 cents per share and converts to one ordinary share	2,257,500	2,805,000

Adjustment has been made to the weighted average number of shares used in calculating diluted earnings per share for the options on issue that have an exercise price below the average market price for the year.

### 24. CAPITAL AND LEASING COMMITMENTS

	2010	2009
	\$	\$

#### Operating Lease Commitments

Non-cancellable operating leases contracted for but not capitalised in the financial statements

Payable

— not later than 1 year	378,386	252,651
— later than 1 year but not later than 5 years	378,310	440,442
— later than 5 years	-	-
	756,696	693,093

Included in the operating lease commitments are non-cancellable property leases with two and three and a half-year terms, with rent payable monthly in advance. Contingent rental provisions within the lease agreements require the minimum lease payments shall be increased by up to 4% per annum. No option exists to renew the leases at the end of the terms.

The leases allows for subletting of all lease areas.

**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 30 JUNE 2010**

**25. SHARE BASED PAYMENTS**

	2010	2009		
<b>(a) Movement in the number of share options held by employees are as follows:</b>				
Opening balance	745,000	467,750		
Granted during the year	577,500	385,000		
Exercised during the year	-	-		
Lapsed during the year	(15,000)	(107,750)		
Closing Balance	1,307,500	745,000		
<b>(b) Details of employee share options outstanding as at end of year:</b>				
Grant Date	Expiry and Exercise Date	Exercise Price		
3 September 2007	30 September 2009 30 September 2010	\$0.40	260,000	260,000
1 May 2008	30 June 2009 30 June 2011	\$0.60	100,000	100,000
3 September 2008	30 September 2010 30 September 2011	\$0.72	260,000	260,000
1 October 2008	31 October 2010 31 October 2011	\$0.80	125,000	125,000
1 July 2009	1 July 2011 30 June 2012	\$0.56	75,000	-
3 September 2009	30 September 2012 30 September 2013	\$0.58	355,000	-
1 October 2009	31 October 2011 31 October 2012	\$0.58	132,500	-
			1,307,500	745,000

Options granted to employees hold no voting or dividend rights and are not transferable.

**(c) Options**

The options outstanding at 30 June 2010 had a weighted average exercise price of \$0.593 (2009: \$0.566) and a weighted average remaining contractual life of 1.2 years (2009: 1.55 years). Exercise prices range from \$0.20 to \$6.00 in respect of options outstanding at 30 June 2010 and 30 June 2009.

The weighted average fair value of the options granted during the year was \$0.1522 (2009: \$0.074).

This price was calculated by using a Black-Scholes option pricing model applying the following inputs:

	2010	2009
Weighted average exercise price	0.5774	\$0.7332
Weighted average life of the option	3.05 years	3.06 years
Underlying share price between	\$0.56 - \$0.58	\$0.42-\$0.54
Expected share price volatility	47.227	67.235
Risk free interest rate	4.0%	6.0%

Historical volatility has been the basis for determining expected share price volatility as it is assumed that this is indicative of future trends, which may not eventuate.

Exercisability of the options has been considered when determining the fair value of the options.

The life of the options is based on the historical exercise patterns, which may not eventuate in the future.

Included under share and option expense in the income statement is \$87,877 (2009: \$139,980), and relates, in full, to equity-settled share-based payment transactions.

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2010

### 25. SHARE BASED PAYMENTS (continued)

#### (d) Shareholdings

Number of Shares held by Key Management Personnel, including shares held by associated entities

	Balance 1.7.09	Net Change /Other	Balance 30.6.10
Peter Neustadt	2,946,023	-	2,946,023
Graham Hurst	1,036,000	(245,000)	791,000
Paul Hopper	-	100,000	100,000
Ralf Barschow	-	-	-
Chris Bedford	-	-	-
John Truitt	8,960	-	8,960
Neil Verdal-Austin	140,000	-	140,000
<b>Total</b>	<b>4,130,983</b>	<b>(145,000)</b>	<b>3,985,983</b>

#### (e) Share based payments

There were no other share-based payment arrangements in the year to 30 June 2010, other than options issued to directors and executives.

#### (f) Options and Rights Holdings

Number of options held by Key Management Personnel, including options held by associated entities

	Balance 1.7.09	Granted as Remuneration/ Exercised	Balance 30.6.10	Total Vested 30.6.10	Total Exercisable	Total Un-exercisable
Paul Hopper	350,000	(300,000)	50,000	50,000	50,000	-
Ralf Barschow	520,000	260,000	780,000	780,000	260,000	520,000
Graham Hurst	350,000	(300,000)	50,000	50,000	50,000	-
John Truitt	75,000	75,000	150,000	150,000	-	150,000
Christopher Bedford	25,000	50,000	75,000	75,000	-	75,000
Peter Neustadt	750,000	-	750,000	750,000	750,000	-
Neil Verdal-Austin	125,000	125,000	250,000	250,000	-	250,000
<b>Total</b>	<b>2,195,000</b>	<b>(90,000)</b>	<b>2,105,000</b>	<b>2,105,000</b>	<b>1,110,000</b>	<b>995,000</b>

\* Expired/lapsed

### 26. EVENTS SUBSEQUENT TO BALANCE DATE

Since the end of the financial year, the directors are not aware of any matter that has significantly affected or may significantly affect the operations of the Company in subsequent financial years.

### 27. CONTINGENT LIABILITIES AND COMMITMENTS

As at 30 June 2010 no contingent liabilities or capital commitments existed.

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2010

### 28: RELATED PARTY DISCLOSURES

Related party transactions fall into the following categories:

(a) Controlled entity

Interests in controlled entities are disclosed in Note 20. The Company engages in transactions with its controlled entities, which are in ordinary course of business at arm's length on a transfer pricing basis.

	2010	2009
	\$	\$

The aggregate amount included in the profit before income tax for the Company that resulted from transactions with non-director related parties are:

License fees	2,183,999	915,396
Revenue from provision of services	628,220	596,953
Interest income	24,875	-

The aggregate amounts receivable from wholly-owned controlled entities by the Company at the reporting date are:

Current receivables	5,517,339	4,210,847
Less impairment	(1,903,589)	(1,046,059)
	3,613,750	3,164,788

(b) Director related entities

(i) During the year consultancy fees of \$108,996 (2009: \$108,996) were paid to Belgove Pty Limited, a company associated with Dr Neustadt.

(ii) In the previous year, SomnoMed Limited transferred to SMH Biomaterial AG, an associated entity, its 50% share of the intellectual property in the SMH Bflex material incurring a loss on transfer of \$53,064. The other 50% share of the intellectual property not owned by Somnomed Limited was also transferred to SMH Biomaterial AG at the same time. This transaction was not at arms length as it was transferred to an associated company. Somnomed Limited still retains the same interest as if the Company had its direct interest in the intellectual property.

(c) Transactions in securities of the Company

During the year directors or entities related to directors acquired under normal commercial terms shares or options in the company as detailed in Note 25. Directors acquired these shares through the public offering, direct issue or on-market purchase.

### 29. KEY MANAGEMENT PERSONNEL COMPENSATION

(a) Names and positions held of Consolidated Entity and Company Key Management Personnel in office at any time during the financial year are:

**Key Management Person**

Peter Neustadt	Chairman — Non-Executive
Graham Hurst	Director — Non-Executive
Paul Hopper	Director — Non-Executive
Ralf Barschow	Chief Executive Officer
Neil Verdal-Austin	Chief Financial Officer
John Truitt	Executive Vice President, North America
Christopher Bedford	General Manager – Production and Technology

**(b) Compensation Practices and Key Management Personnel Compensation**

Details of compensation practices and key management personnel compensation are disclosed in the Directors' Report, which accompanies these financial statements.

Details of management personnel compensation shares and options are disclosed in Note 25.

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2010

### 30. FINANCIAL INSTRUMENTS

#### Credit Risk

##### *Exposure to Credit Risk*

The carrying amount of financial assets represents the maximum credit exposure. The maximum exposure to credit risk at the reporting date was:

	2010	2009
	\$	\$
Cash and equivalents	4,293,676	4,008,934
Trade receivables	1,295,955	1,180,490
Forward exchange contracts	54,174	
Other receivables	233,390	64,059
	5,877,195	5,253,483

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

United States	916,116	911,926
Europe	176,532	117,296
Asia Pacific	203,307	151,268
	1,295,955	1,180,490

##### *Impairment Losses*

The ageing of the trade receivables at the reporting date was:

#### **Gross receivables**

Not past due date	917,381	715,455
Past due 0 – 30	169,650	306,053
Past due 31 – 60	122,630	91,045
Past due 60 – 90	47,490	32,955
Past due 90 days and over	114,338	106,246
	1,371,489	1,251,754
Impairment	(75,534)	(71,264)
<b>Trade receivables net of impairment loss</b>	1,295,955	1,180,490

The movement in the allowance for impairment in respect of trade receivables during the year was as follows:

Balance at 1 July	(71,264)	(19,022)
Impairment loss recognised	(4,270)	(52,242)
<b>Balance at 30 June</b>	(75,534)	(71,264)

Impairment losses recognised in the year relate to significant individual customers, which have been assessed as impaired under the Consolidated Entity's accounting policy as detailed in Note 3(h).

Based upon past experience, the Consolidated Entity believes that no impairment allowance other than as provided in these accounts is necessary in respect of trade receivables not past due.

The allowance accounts used in respect of trade receivables are used to record impairment losses unless the Consolidated Entity is satisfied that not recovery of the amount owing is possible; at that point, the amount considered non-recoverable is written off against the financial asset directly.

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2010

### 30. FINANCIAL INSTRUMENTS (continued)

#### Currency Risk

Consolidated Entity's exposure to foreign currency risk was as follows, based upon notional amounts:

Amounts local currency	SGD	PHP	JPY	USD	EUR	CHF
<b>2010</b>						
Cash and cash equivalents	2,960	45,882	10,459	1,034,332	609,965	-
Trade receivables	-	-	7,704	950,172	205,787	-
Trade payables	(3,743)	(46,430)	(9,857)	(965,627)	(167,606)	-
<b>Gross balance sheet exposure</b>	<b>(783)</b>	<b>(548)</b>	<b>8,306</b>	<b>1,018,877</b>	<b>648,146</b>	<b>-</b>

Amounts local currency		JPY	USD	EUR	CHF
<b>2009</b>					
Cash and cash equivalents		1,220	855,819	121,347	3,074
Trade receivables		-	938,899	117,296	-
Trade payables		-	(528,770)	(52,338)	(92,455)
<b>Gross balance sheet exposure</b>		<b>1,220</b>	<b>1,265,948</b>	<b>186,305</b>	<b>(89,381)</b>

Somnomed enters into forward exchange contracts to hedge its exposure to the USD. The amounts of forward cover taken are in accordance with approved policy and internal forecasts.

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

	Foreign exchange rates		Gross Value	
	2010	2009	2010	2009
Sell USD				
Not later than one year	-	-	886,815	-
Weighted average exchange rates contracted	0.7893	-	-	-

The following significant exchange rates applied to the Consolidated Entity during the year:

	Average Rate		Reporting date spot rate	
	2010	2009	2010	2009
AUD = 1				
USD	0.8762	0.7585	0.8407	0.8064
EUR	0.6377	-	0.6872	0.5745
CHF	-	0.7983	-	0.8761
JPY	80.001	-	74.365	-
PHP	41.051	-	39.140	-

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2010

### 30. FINANCIAL INSTRUMENTS (continued)

#### Interest Rate Risk

##### Profile

At the reporting date, the interest rate profile of the Consolidated Entity's interest bearing financial instruments was:

Carrying amount	2010	2009
	\$	\$
<b>Variable rate instruments</b>		
Financial assets	1,961,842	2,378,462

#### Liquidity Risk

The following are the contractual maturities of the Consolidated Entity's financial assets and liabilities including estimated interest payments.

2010	Effective interest rate p.a.	Carrying amount \$	Less than 1 year	1-5 years	More than 5 years
Cash and cash equivalents	2.15%	4,293,676	4,293,676	-	-
Receivables	-	1,583,519	1,583,519	-	-
Payables	-	(1,874,340)	(1,872,625)	(1,715)	-
<b>Total</b>	-	4,002,855	4,004,570	(1,715)	-

  

2009	Effective interest rate p.a.	Carrying amount \$	Less than 1 year	1-5 years	More than 5 years
Cash and cash equivalents	4.25%	4,008,934	4,008,934	-	-
Receivables	-	1,426,190	1,426,190	-	-
Payables	-	(1,455,862)	(1,455,862)	-	-
<b>Total</b>	-	3,979,262	3,979,262	-	-

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2010

### 30. FINANCIAL INSTRUMENTS (continued)

#### Sensitivity Analysis

In managing interest rate and currency risks, the Consolidated Entity aims to reduce the impact of short-term fluctuations on the Consolidated Entity's earnings. Over the longer term however, permanent changes in foreign exchange and interest rates will have an impact on the result.

For the year ended 30 June 2010, it is estimated that a general increase of one percent in interest rates would have increased the Consolidated Entity's profit after income tax and equity by approximately \$42,000 and for the year ended 30 June 2009 the effect would have been to decrease the Consolidated Entity's loss after income tax and equity by approximately \$52,000. A one percent decrease in interest rates would have had the equal but opposite effect on the Consolidated Entity's profit/(loss) and equity.

It is estimated that a general increase of ten percent in the value of the AUD against other foreign currencies would have increased the Consolidated Entity's profit for the year ended 30 June 2010, and increase the Consolidated Entity's equity by approximately \$165,000. For the year ended 30 June 2009 the effect would have been to decrease the Consolidated Entity's loss and increase the equity by \$180,000.

It is estimated that a general decrease of ten percent in the value of the AUD against other foreign currencies would have decreased the Consolidated Entity's profit for the year ended 30 June 2010, and decrease the Consolidated Entity's equity by approximately \$81,000. For the year ended 30 June 2009 the effect would have been to increase the Consolidated Entity's loss and decrease the equity by \$180,000.

#### Fair Values

The fair values of financial assets and liabilities, together with carrying amounts shown in the balance sheet are as follows:

	2010		2009	
	\$		\$	
Consolidated	Carrying amount	Fair value	Carrying amount	Fair value
Cash and equivalents	4,293,676	4,293,676	4,008,934	4,008,934
Trade and other receivables – current	1,583,519	1,583,519	1,244,356	1,244,356
Trade and other payables	(1,874,340)	(1,874,340)	(1,455,862)	(1,455,862)
<b>Total</b>	<b>4,002,855</b>	<b>4,002,855</b>	<b>3,797,428</b>	<b>3,797,428</b>

#### Basis for determining fair values

The following summarises the significant methods and assumptions used in estimating the fair values of financial instruments reflected in the table above.

#### Non-derivative financial assets and liabilities

The fair value of cash, receivables, payables and short-term borrowings is considered to approximate their carrying amount because of their short maturity.

#### Fair value hierarchy

The table below analyses financial instruments carried at fair value, by valuation method. The different levels have been defined as follows:

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

	Level 2	Total
<b>30 June 2010</b>		
<b>Derivative financial assets</b>		
Forward exchange contracts	54,175	54,175
<b>30 June 2009</b>		
<b>Derivative financial assets</b>		
Forward exchange contracts	-	-

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2010

### 31. PARENT ENTITY DISCLOSURES

At and throughout the financial year ended 30 June 2010, the parent company was Somnomed Limited.

	<b>Company</b>	
	<b>30 June 2010</b>	<b>30 June 2009</b>
	<b>\$</b>	<b>\$</b>
<b>Result of the parent entity</b>		
Net profit/(loss)	3,074	(960,980)
Other comprehensive income/(loss)	-	-
<b>Total comprehensive income</b>	<b>3,074</b>	<b>(960,980)</b>
<b>Financial position of the parent entity at year end</b>		
Current assets	6,958,925	6,372,456
Total assets	7,698,928	7,175,005
Current liabilities	735,176	738,203
Total liabilities	735,176	738,203
<b>Total equity of the parent entity comprising of:</b>		
Issued capital	23,706,829	23,270,829
Share option reserve	1,374,796	1,286,919
Accumulated losses	(18,117,872)	(18,120,946)
<b>Total Equity</b>	<b>6,963,752</b>	<b>6,436,802</b>

### Parent entity contingencies

There are no contingent liabilities and future commitments in respect to the Parent Entity.

**SOMNOMED LIMITED**  
ACN 003255221  
**DIRECTORS' DECLARATION**

The directors of the company declare that:

1. the financial statements and notes, as set out on pages 18 to 46 are in accordance with the Corporations Act 2001:
  - a. comply with Accounting Standards and the Corporations Regulations 2001; and
  - b. give a true and fair view of the financial position as at 30 June 2010 and of the performance for the year ended on that date of the company and Consolidated Entity;
2. The Chief Executive Officer and Chief Finance Officer have each declared that:
  - a. the financial records of the company for the financial year have been properly maintained in accordance with section 286 of the Corporations Act 2001;
  - b. The financial statements and notes for the financial year comply with the Accounting Standards; and
  - c. The financial statements and notes for the financial year give a true and fair view.
3. in the directors' opinion there are reasonable grounds to believe that the company will be able to pay its debts as and when they become due and payable.

This declaration is made in accordance with a resolution of the Board of Directors.



**Peter Neustadt**

**Chairman**

Dated 24 September 2010



**STIRLING INTERNATIONAL**  
CHARTERED ACCOUNTANTS

**INDEPENDENT AUDIT REPORT TO THE MEMBERS OF  
SOMNOMED LIMITED**

**Report on the Financial Report**

We have audited the accompanying financial report of SomnoMed Limited (the company) and the consolidated entity, which comprises the balance sheet as at 30 June 2010, and the income statement, statement of comprehensive income, statement of changes in equity and statement of cash flows for the year ended on that date, a summary of significant accounting policies and other explanatory notes 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.

*Directors' Responsibility for the Financial Report*

The directors of the company are responsible for the preparation and fair presentation of the financial report in accordance with Australian Accounting Standards (including the Australian Accounting Interpretations) and the *Corporations Act 2001*. This responsibility includes establishing and maintaining internal control relevant to the preparation and fair presentation of the financial report that is free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances. In Note 2, the directors also state, in accordance with Accounting Standard AASB 101: Presentation of Financial Statements, that compliance with the Australian equivalents to International Financial Reporting Standards (IFRS) ensures that the financial report, comprising the financial statements and notes, complies with IFRS.

*Auditor's Responsibility*

Our responsibility is to express an opinion on the financial report based on our audit. We conducted our audit in accordance with Australian Auditing Standards. These Auditing Standards require that we comply with relevant ethical requirements relating to audit engagements and plan and perform the audit to obtain reasonable assurance whether the financial report is free from material misstatement.

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 judgment, 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 and fair presentation of the financial report 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. 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 believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

*Independence*

In conducting our audit, we have complied with the independence requirements of the *Corporations Act 2001*. We confirm that the independence declaration required by the *Corporations Act 2001*, provided to the directors of SomnoMed Limited, would be in the same terms if provided to the directors as at the date of this auditor's report.

**INDEPENDENT AUDIT REPORT TO THE MEMBERS OF  
SOMNOMED LIMITED**

*Auditor's Opinion*

In our opinion:

- a. the financial report of SomnoMed Limited is in accordance with the *Corporations Act 2001*, including:
  - i. giving a true and fair view of the company's and consolidated entity's financial position as at 30 June 2010 and of their performance for the year ended on that date; and
  - ii. complying with Australian Accounting Standards (including the Australian Accounting Interpretations) and the Corporations Regulations 2001;
- b. the financial report also complies with International Financial Reporting Standards as disclosed in Note 2.

**Report on the Remuneration Report**

We have audited the Remuneration Report included in the report of the directors for the year ended 30 June 2010. The directors of the company are responsible for the preparation and presentation of the Remuneration Report in accordance with s 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 the Australian Auditing Standards.

*Auditor's Opinion*

In our opinion the Remuneration Report of SomnoMed Limited for the year ended 30 June 2010, complies with s 300A of the Corporations Act 2001.

Stirling International  
Chartered Accountants



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Peter Turner  
St James Centre 111 Elizabeth St Sydney 2000  
24 September 2010

**AUDITOR'S INDEPENDENCE DECLARATION  
UNDER SECTION 307C OF THE CORPORATIONS ACT 2001  
TO THE DIRECTORS OF SOMNOMED LIMITED**

I declare that, to the best of my knowledge and belief, during the year ended 30 June 2010 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.

Stirling International  
Chartered Accountants



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Peter Turner  
  
24 September 2010  
St James Centre 111 Elizabeth St Sydney 2000

## ADDITIONAL INFORMATION

### 1. Shareholding

a. Distribution of Shareholders	Number
Category (size of Holding)	
1-1,000	383
1,001-5,000	261
5,001-10,000	137
10,001-100,000	265
100,001 and over	51
	1,097

b. The number of shareholdings held in less than marketable parcels is 295

c. The names of the substantial shareholders listed in the holding company's register as at 15 September 2010 are:

Shareholder	Number of Ordinary Shares	Percentage
Dottie Investments Pty Ltd	3,732,779	9.258%
Golden Words Pty Ltd	3,327,932	8.25%
Belgove Pty Limited	3,371,023	8.36%

### d. Voting Rights

Each ordinary share is entitled to one vote when a poll is called, otherwise each member present at a meeting or by proxy has one vote on a show of hands.

### e. 20 Largest Shareholders — Ordinary Shares as at 15 September 2010

Name	No. of Ordinary Fully Paid Shares Held	% Held of Issued Ordinary Capital
1. Dottie Investments Pty Ltd	3,732,779	9.258%
2. Belgove Pty Limited	3,371,023	8.361%
3. Golden Words Pty Ltd	3,177,932	7.882%
4. UBS Wealth Management	1,763,816	4.375%
5. ANZ Nominees Limited	1,453,039	3.604%
6. Ginga Pty Ltd	1,305,654	3.238%
7. Carnethy Evergreen Pty Ltd <Carnethy Evergreen Fund A/C>	1,250,000	3.100%
8. R E M Medical Pty Ltd <Cocoon Super Fund Account >	1,216,656	3.018%
9. EST Dr Richard Palmisano	1,106,000	2.743%
10. M F Custodians Ltd	954,474	2.367%
11. Pavona Pty Ltd	880,706	2.184%
12. Timbina Pty Ltd <Timbina Super Fund A/C>	761,737	1.889%
13. Atul Mehta & Roopa Mehta <Roma Super Fund A/C>	650,000	1.612%
14. Atlas Ventures (Nominee) Pty Limited	526,316	1.305%
15. Roslyndale Pty Limited	520,684	1.291%
16. Mr Graham Hurst and Mrs Susan Hurst	477,000	1.183%
17. Ryan Superannuation Nominees	423,212	1.050%
18. Tunend Pty Ltd	382,000	0.947%
19. Pavona Pty Ltd <Penn Super Fund>	326,321	0.809%
20. Mr Graham Hurst	314,000	0.779%
	<b>24,593,349</b>	<b>60.995%</b>

# CORPORATE DIRECTORY

## Registered Office

Level 3  
20 Clarke St Crows Nest 2065  
Telephone: (02) 9467 0400

## Directors

Peter Neustadt	Non-executive Chairman
Paul Hopper	Non-executive Director
Graham Hurst	Non-executive Director

## Chief Executive Officer

Ralf Barschow

## Chief Financial Officer

Neil Verdal-Austin

## Company Secretary

Terence Flitcroft

## Patent Attorneys

Spruson & Ferguson

## Banker

Westpac Banking Corporation

## Auditors

Stirling International

## Share Registry

Registries Limited  
SYDNEY NSW 2000

(GPO Box 3993 Sydney NSW 2001)

Telephone (02) 9290 9600

Facsimile (02) 9279 0664

[www.registriesltd.com.au](http://www.registriesltd.com.au)

## Company Website

[www.somnomed.com.au](http://www.somnomed.com.au)

## HEAD OFFICE

### **SomnoMed Limited**

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Australia

Phone: 1800 445 660

Fax: +61 2 9467 0467

## EUROPE

### **SomnoMed Europe AG**

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CH-8032 Zürich  
Switzerland

### **SomnoMed Nordic AB**

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115 26 Stockholm  
Sweden

## ASIA

### **SomnoMed Japan Corporation**

La-ju Oimachi,6F  
Oi 4-13-17, Shinagawa-ku  
Tokyo, 140-0014  
Japan

### **SomnoMed Singapore Pte Ltd**

8 Temasek Boulevard,  
#35-03 Suntec Tower 3,  
Singapore 038988

## NORTH AMERICA

### **SomnoMed Inc.**

3537 Teasley Lane  
Denton, Texas 76210  
U.S.A.