

**Consolidated financial statements  
of Carl Zeiss Meditec AG (US GAAP)**

2003/2004

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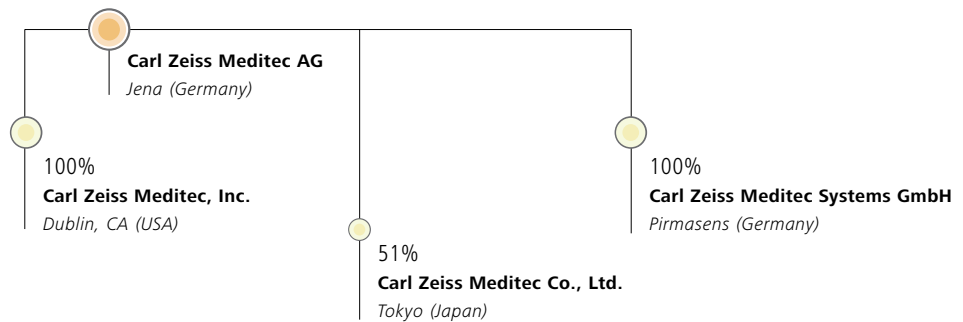
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# Consolidated management report for the financial year 2003/2004

## Executive summary

Carl Zeiss Meditec AG, Jena, is the parent company of the Carl Zeiss Meditec Group (the "Group", "Carl Zeiss Meditec"). Together with its operative companies, as of 30 September 2004 the Carl Zeiss Meditec Group had the following structure:



The take-over of the glaucoma diagnosis specialist Laser Diagnostic Technologies, Inc., San Diego, USA, ("LDT"), which was announced after the balance sheet date, and its integration into the Carl Zeiss Meditec Group, has not been taken into account as a number of resolutions still have to be adopted by the respective committees. Further details on the acquisition of LDT are to be found in the supplementary report.

Despite negative exchange rate effects, consolidated sales almost reached the level seen in the previous year. They totalled € 234.9 million (previous year: € 235.7 million). Had exchange rates remained on the previous year's level, sales would have been € 249.9 million - an increase of 6.0% over the previous year. Due to the further optimisation of the product mix and reductions in costs of revenues, the consolidated gross margin increased to 46.4% (previous year: 43.5%).

Earnings before interest and tax (EBIT) significantly improved by 6.5% over the previous year (€ 24.7 million) to € 26.3 million. The EBIT margin also significantly improved. In the financial year 2003/2004 it amounted to 11.2%, following on from 10.5% in the previous year.

Consolidated net income was almost double the previous year's figure. It amounted to € 12.6 million (previous year: € 6.6 million). Earnings per share increased to € 0.44 (previous year: € 0.25).

Thanks to a clear reduction in accounts receivable and inventories, coupled with a positive business development, the cash flow from operating activities repeatedly improved in the period under review, rising by 12.6% to € 31.6 million (previous year: € 28.1 million).

The net cash and cash equivalents (cash on hand and credits with the group treasury of Carl Zeiss AG) reached a record level of € 77.1 million (previous year: € 57.1 million).

## Business report

### 1. Underlying conditions for economic development<sup>1</sup>

The powerful upturn that lasted until the spring of 2004 has since slowed down. Growth in the USA and China, in particular, has tailed off considerably. In both countries the reins have been pulled in on the prevailing monetary policy. In the USA financial policy moves to stimulate the economy have now run their course, and in China administrative measures have been taken to rein in the exuberant economy.<sup>2</sup>

The economic recovery in the euro-zone stabilised in the financial year 2003/2004. Thus, the gross domestic product in real terms rose to a significantly greater degree in the first six months of 2004 than it had in the last six months of 2003. Although there were considerable differences between the individual EU member states with respect to the strength of growth and also its causes, on the whole it may be stated that the economic recovery in this region was fuelled to a greater degree by exports than by an increase in domestic demand.<sup>3</sup>

The recovery in the German economy – analogous to developments throughout the euro-zone – was reinforced in the period under review. Thus economic research institutes such as Deutsches Institut für Wirtschaftsforschung ("DIW") regard "the ongoing stagnation which set in with the economic collapse crash in the year 2000"<sup>4</sup>, as having been overcome. The motor for growth is once again exports, however. Domestic demand – and here above all private and state spending – continue to stagnate. The reasons for this stagnating demand lie in rising energy prices and consumer uncertainty arising from the diverse reform plans, the majority of which are yet to be implemented.

Business activities in the regions are being dampened by the major rise in oil prices. Moreover, exports from the euro-zone have been burdened by a considerable rise in the value of the euro over the US dollar.

<sup>1</sup> Deutsches Institut für Wirtschaftsforschung (German Institute for Economic Research), Berlin (Publ.): Weekly Report No. 43/2004 "The Situation of the Global and German Economies in Autumn 2004", 21.10.2004, Berlin

<sup>2</sup> Cf. *ibid.*, p. 629-637

<sup>3</sup> Cf. *ibid.*, p. 638ff

<sup>4</sup> *Ibid.* p. 645

## 2. Structure of the consolidated financial statements

The following aspects must be borne in mind with regard to the structure of the consolidated financial statements:

- Expansion of the reporting entity: On 17 December 2003 Carl Zeiss Meditec acquired a 100% interest in hiko medical communication GmbH of Pirmasens, Germany ("hiko"), a company specialising in the development of software for medical technology. Accordingly, the activities of the former hiko, now operating under the name Carl Zeiss Meditec Systems GmbH, are included in the consolidated financial statements of Carl Zeiss Meditec from this date onwards.
- Reporting of discontinued operations: With effect from 1 May 2003, in the financial year 2002/2003 Carl Zeiss Meditec sold off the Aesthetic and Dental divisions that were not part of its core business. In accordance with the US accounting rules set forth in SFAS No. 144, this disposal was classified as "discontinued operations". Accordingly, the contributions to sales and expenses generated in this sector were aggregated in the previous year's consolidated income statement and disclosed separately. The revenue from the sale of business units is shown at the end of the income statement ("Consolidated net income from discontinued operations").

## 3. Development of sales

In the financial year 2003/2004 Carl Zeiss Meditec posted consolidated sales of € 234.9 million, a figure similar to that seen in the previous year (€ 235.7 million). The organic sales growth within the Group was thus able to compensate for negative exchange rate effects, which resulted above all from the decrease in value of the US dollar over the euro. Whereas one US dollar cost an average of 0.93 euro in the financial year 2002/2003, this figure fell by 0.11 euro in the period under review to an average of 0.82 euro. Accordingly, if the development of the consolidated sales is compared with the previous year on the basis of constant exchange rates, there would have been an improvement of 6.0% to € 249.9 million over the financial year 2002/2003.

Furthermore, if the consolidated sales attained in the previous year from OEM contracts<sup>5</sup> terminated at the beginning of the financial year 2003/2004 are adjusted, on a comparable basis to the previous year ("*like for like*") the adjusted growth in sales in the Group is 12.3%.

<sup>5</sup> The Group manufactures products for other companies within the framework of Original Equipment Manufacturing contracts ("*OEM contracts*"), who then sell these to end customers under their own brand names. The terminated contracts were originally concluded by the American subsidiary Carl Zeiss Meditec, Inc., so as to utilise available production capacities.

### Sales by business segment

Consolidated sales in the Laser business unit rose considerably. In the reporting period sales of € 44.1 million were attained. This corresponds to an increase of 27.7% over the previous year (€ 34.5 million). The share of this business segment in the consolidated sales has thus increased from 14.6% in the financial year 2002/2003 to 18.8% in the financial year 2003/2004. The major contribution to this was made by the positive development in sales in the field of refractive lasers. The main focus of sales, in this respect, was on Europe and Asian growth regions such as China. Furthermore, business with the other laser systems also developed dynamically. The VISULAS™ 532s and the VISULAS™ 532s Combi for the treatment of retinal diseases and glaucoma were successful in Europe, above all. Moreover, sales with the VISULAS™ 690s system, which is used within the framework of a so-called photodynamic therapy in conjunction with the Novartis drug Visudyne® for the treatment of age-related macular degeneration (AMD), rose in Japan in the period under review. The foundations for this were laid by the granting of product approval by the Japanese Ministry of Health in December 2003 and the publication in June 2004 of the decision by this ministry to reimburse the costs for AMD treatments with the VISULAS™ 690s and Visudyne®

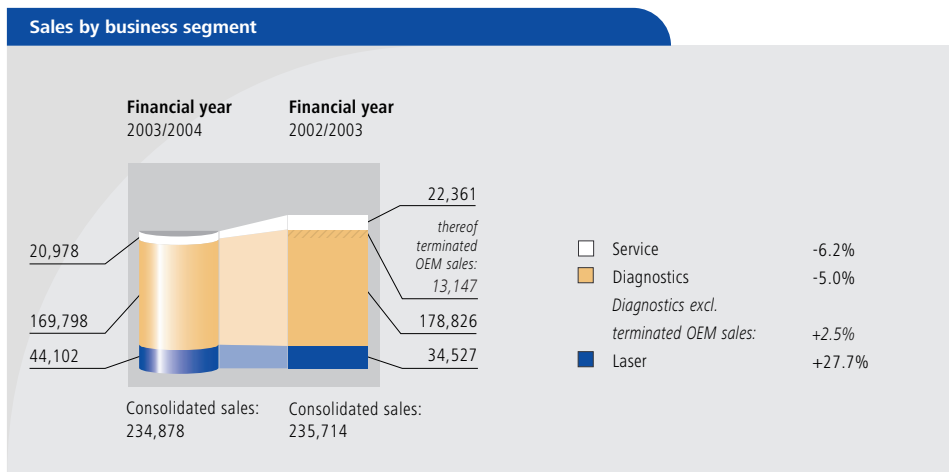
Consolidated sales in the Diagnosis business unit decreased by 5.0% over the previous year as a consequence of exchange rates and the termination of the above-mentioned OEM contracts. In the reporting period these amounted to € 169.8 million (previous year: € 178.8 million). The mainstays of sales in this segment were the systems STRATUSocT™, IOLMaster® and the Humphrey® Field Analyzer. The most important markets for the STRATUSocT™ diagnostic system in the reporting period were the USA and Japan. Moreover, consolidated sales with this product rose in Europe. The unique technology – optical coherence tomography – upon which the STRATUSocT™ is based enables the rendering of real-time, cross-section views of the neurofibril layers of the eye. In this way serious eye diseases like glaucoma and several retinal disorders can be diagnosed earlier than hitherto. The most significant sales markets for the IOLMaster®, with which the eye can be measured contact-free and precisely prior to an operation for cataracts, were Europe and the USA. The Humphrey® Field Analyzer HFA, which has established itself as the "gold standard" for the diagnosis of glaucoma, saw significant sales in the USA and Japan. Further mainstays of sales were the diagnostic system Humphrey® FDT for the routine diagnosis of the field of vision within the framework of glaucoma check-ups and the fundus cameras FF 450 and VISUCAM™ *lite*, with which the ocular fundus may be examined precisely.

Sales in the Service business unit decreased by 6.2% to € 21.0 million from € 22.4 million in the previous year. The share of the sales from the Service unit in consolidated sales thus decreased slightly, from 9.5% in the previous year to 8.9% in the financial year 2003/2004. A significant reason for this development lays in the guarantee periods granted for the many new products launched on the market by the Company, such as the refractive laser MEL 80™, and during which there are generally only low service revenues. However, in the future the Group expects service sales to rise as customers usually enter into maintenance agreements for more complex products once the guarantee period has expired.

Sales by business segment in the financial years 2003/2004 and 2002/2003 developed as summarised in Figure 1.

Figure 1: Sales by business segment in the financial years 2003/2004 and 2002/2003

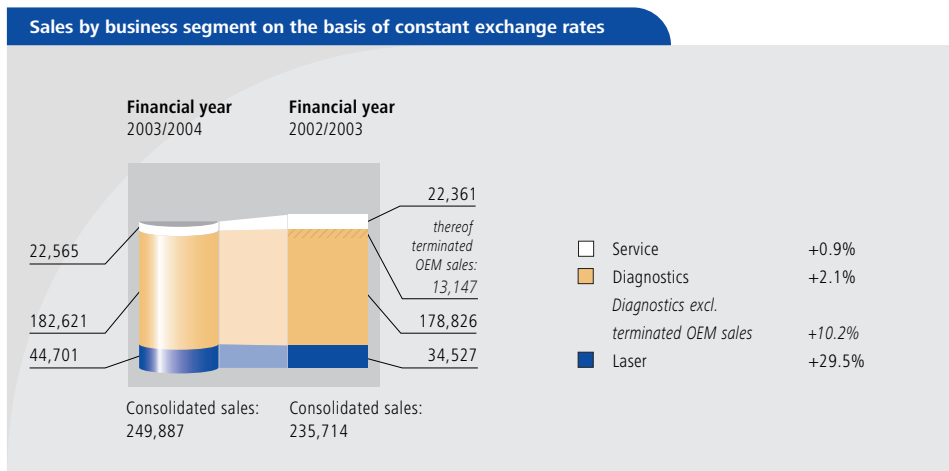
(in € '000)



On the basis of constant exchange rates over the previous year all of the Group's business units would have attained an increase in sales. If the consolidated sales are also adjusted for those sales with diagnostic systems attained in the previous year with OEM supplies, the Group's largest business unit would have posted an increase in sales of 10.2% in the period under review compared to the financial year 2002/2003. Figure 2 shows the distribution of consolidated sales by business segment on the basis of constant exchange rates.

Figure 2: Sales by business segment in the financial years 2003/2004 and 2002/2003 on the basis of constant exchange rates

(in € '000)



The distribution of sales by region in the period under review reflects the macro-economic trends shown in the section "1. Underlying conditions for economic development". The greatest impetus for sales came from the Asian/Pacific region. In this region, consolidated sales rose by 17.4%, to € 65.5 million (previous year: € 55.8 million). With an upturn of 8.2% a comparatively high growth rate was also attained in Germany. In the period under review the Group posted sales of € 17.7 million in Germany (previous year: € 16.4 million), something that is, above all, due to the excellent development of sales in the fourth quarter of the financial year 2003/2004. The development of the consolidated sales in Germany may be interpreted as an initial indication that the current reservation with replacement investment is being reversed. Moderate sales growth was attained in Europe (excluding Germany), where the sales revenues increased by 4.5%, to € 41.9 million (previous year: € 40.1 million). Sales in the Americas region, which encompasses the USA above all, decreased by 11.1%, from € 123.5 million in the previous year to € 109.8 million. The reasons for this are the weakness of the US dollar over the euro, and the loss of sales of € 13.1 million attained in the previous year with OEM supplies. Figure 3 shows the development of consolidated sales by region.

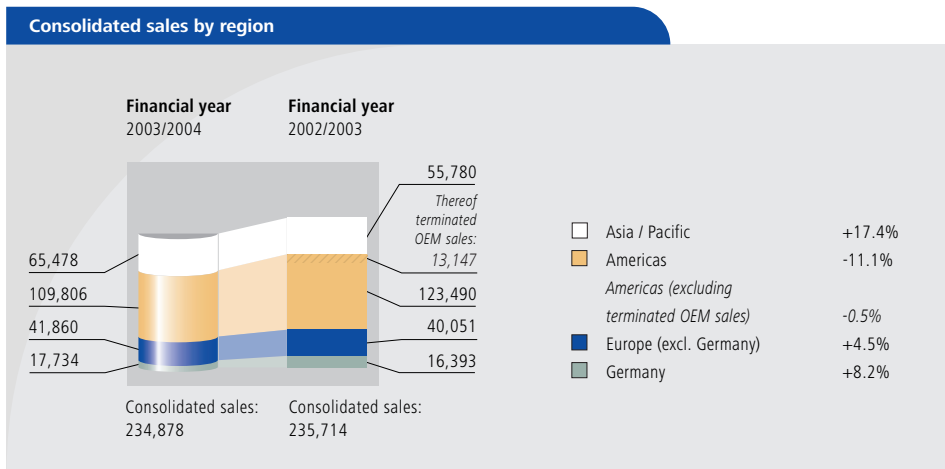
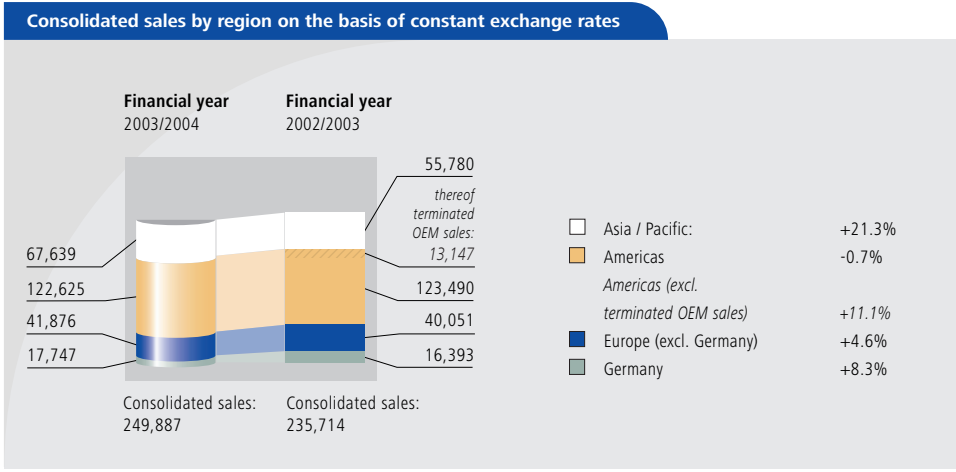


Figure 3:  
Consolidated sales by region  
in the financial years  
2003/2004 and 2002/2003  
  
(in € '000)

On a comparable basis with the previous year, namely with constant exchange rates and following the adjustment for the OEM sales in the financial year 2003/2004, it may be seen that the Group has been able to considerably expand its regional market position, and in particular in the USA, the world's largest medical market. The adjusted increase in sales here would have been 11.1%. In the Asia/Pacific Rim region the growth in sales would have been 21.3%, and thus much greater than reported. Figure 4 shows the development of consolidated sales by region on the basis of constant exchange rates.

Figure 4: Consolidated sales by region in the financial years 2003/2004 and 2002/2003 on the basis of constant exchange rates (in € '000)

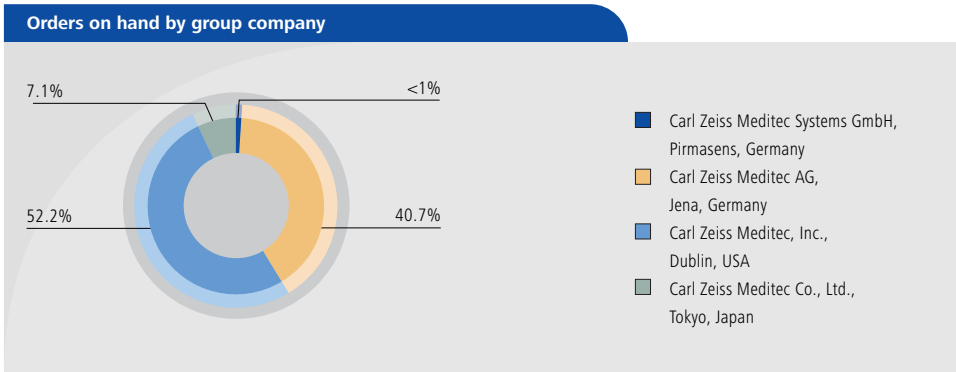


#### 4. Orders on hand

As of 30 September 2004 Group's orders on hand totalled € 13.6 million (previous year: € 13.2 million). As in the previous year, Carl Zeiss Meditec believes there is a continuing trend towards customers placing orders at short notice.

Figure 5 shows the distribution of orders on hand as at the individual group companies of the balance sheet date.

Figure 5: Orders on hand by group company (30 September 2004)



## 5. Production planning and production

The Group has two production sites. These are located in Jena, Germany and Dublin, USA.

The Group's core competencies embrace the development of new technologies, products and applications (cf. Research and Development Report) and the manufacture of key components. The main focus of product manufacturing by the Carl Zeiss Meditec Group is on the assembly of system components. More than two thirds of the parts or components required in Jena are purchased from external suppliers. The remaining third is divided equally between other members of the Carl Zeiss AG and the Group's own component manufacturing facilities. A large number of the parts and system components used in Dublin are purchased from external suppliers.

In the financial year 2003/2004 the Group further extended and optimised its production processes. Moreover, the assembly processes were further optimised for those systems produced in large numbers. At the sites in Jena and Dublin production lines were also established for the new products launched on the market in the financial year.

Production planning in Jena is based on the *rolling forecast* method used by the sales partners. This method requires the latter to prepare a rolling sales forecast as a basis for ordering individual items and manufacturing components. For the purposes of restricting stock-keeping to a minimum, final assembly is usually performed to customer orders. Products at Dublin are made to meet the orders of marketing partners according to the *demand-flow* principle.

## 6. Development of manufacturing capacities

The Carl Zeiss Meditec Group compensates for fluctuations in demand by flexible deployment of production personnel. One prerequisite for this is an appropriate training system, by which the employees are qualified for work on the different production lines.

## 7. Procurement

As described under "5. Production planning and production", products are assembled almost exclusively to customer orders submitted. The purpose of this is to keep stocks as low as possible. Accordingly, the respective components are called up from suppliers shortly before the production date.

Moreover, the Group made further progress in the optimisation of its inventories in the financial year 2003/2004. Thus, so-called consignment warehouses were established with other main suppliers at the Jena location. These are stock warehouses which are owned by the respective supplier and are integrated into the product process of the Group. The necessary components are called up as required and invoiced. Furthermore, the organisation of restocking for these warehouses is entirely in the hands of the suppliers.

The Group attaches great significance to long-term partnerships with its suppliers. Suppliers are subject to regular qualification audits in order to ensure consistently high quality levels, and also with purchased components and parts.

## 8. Quality management

Official registrations and approvals are demanded by the majority of markets as a prerequisite for the marketing of medical products. Accordingly Carl Zeiss Meditec has had its individual group companies registered with the responsible national agencies. In order to successfully attain approvals the quality management system of the Group is regularly audited and certified by DQS GmbH Deutsche Gesellschaft zur Zertifizierung von Managementsystemen in accordance with ISO 9001 & 13485, Appendix II & V of the Directive 93/42/EEC and the *Canadian Medical Device Regulation* (CMDR).

The quality management system of the Carl Zeiss Meditec Group also conforms with the requirements of the U.S. legislation 21 C.F.R. part 820, *Quality Systems Regulation*.

## 9. Registrations and approvals

The Group's products are fundamentally intended for marketing worldwide. For this reason, the design features, materials and components employed, as well as the interfaces of all devices and systems, are all chosen at the outset so that they can be used anywhere in the world.

With the exception of the refractive laser MEL 80™, for which the approval procedure in the USA and Japan is still pending, the Group's complete range of products has been approved in all major countries of the world.

## 10. Personnel

As of 30 September 2004 the Carl Zeiss Meditec Group employed a workforce of 796 (previous year: 752). In addition there were 23 trainees in Germany. Partially retired employees in Germany were not included in this figure. The increase in the number of employees results from the take-over of hiko medical communication GmbH as of 17 December 2003 (cf. also Section "12. Events of particular significance").

On an annual average a total of 801 employees were employed by the Group in the financial year 2003/2004 (previous year: 798 employees). Total personnel expenses<sup>6</sup> in the reporting period stood at € 60.4 million (previous year: € 61.5 million). Personnel expenses as a ratio of consolidated sales are thus 25.7% (previous year: 26.1%).

Figure 6 provides an overview of the personnel structure at the Carl Zeiss Meditec Group as of 30 September 2004.

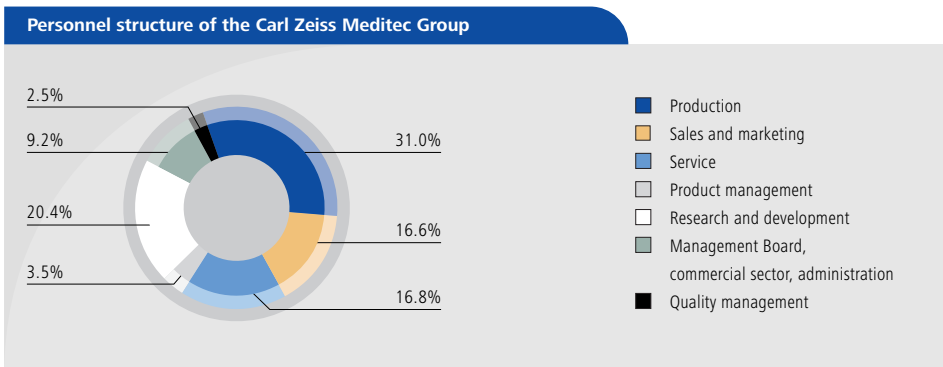


Figure 6:  
Personnel structure of  
the Carl Zeiss Meditec Group  
as of 30 September 2004

## 11. Environmental protection

Within the framework of its business activity the Group complies with all the relevant environmental protection provisions.

There is no direct or indirect risk to the environment from the Group's products or production methods.

<sup>6</sup> This item encompasses wages and salaries, social security and retirement pension payments.

## 12. Events of particular significance

On 17 December 2003 Carl Zeiss Meditec announced that the Group had acquired a 100% interest in its long-standing alliance partner hiko medical communication GmbH in Pirmasens. hiko medical communication GmbH has been trading as Carl Zeiss Meditec Systems GmbH since 29 June 2004.

Carl Zeiss Meditec Systems GmbH specialises in the development of medical software solutions, and under the name VISUPACT™ it markets a successful product that enables central filing and management of diagnostic and treatment data by eye specialists and clinics.

With this acquisition a further major step was taken towards implementing the corporate strategy. The Group has thus secured the necessary resources and know-how in order to be able to offer customers cross-platform software solutions for ophthalmic applications.

## 13. Net worth

### a) Statement of net worth

The consolidated balance sheet total of Carl Zeiss Meditec as of 30 September 2004 stood at € 215.4 million. Compared to the previous year (€ 205.8 million) this constitutes an increase of 4.7%. This increase is essentially due to a rise of 10.5% in the liquid funds to € 49.7 million (previous year: € 45.0 million), as well as to a considerable rise in the credit with the group treasury of Carl Zeiss AG. This credit, which is disclosed under "Accounts receivable due from affiliated companies" totalled € 27.4 million (previous year: € 12.1 million) as of 30 September 2004. The Carl Zeiss Meditec Group may dispose of the funds, which are invested at the customary market conditions, at short notice. Furthermore, the item "Goodwill" increased by € 5.0 million to € 16.1 million. The reason for this is the acquisition of hiko medical communication GmbH (cf. also Section "12. Events of particular significance"). In total, this more than compensated for the various contracting effects on the assets side of the consolidated balance sheet. These effects include:

- A significant reduction in trade accounts receivable due to further optimisation of collection management and a further conservative valuation of long-standing receivables. This balance sheet item decreased by 13.5%, from € 30.3 million as of 30 September 2003 to € 26.2 million as of 30 September 2004.
- The reduction in the inventories following an improvement in stock management (cf. Sections "5. Production planning and production" and "7. Procurement"): Inventories were 11.6% down on last year at € 34.1 million (previous year: € 38.6 million).
- The reduction of "Other assets": Compared to the previous year this balance sheet item declined by € 3.3 million to € 1.2 million. This is essentially due to the payment of the final purchase price instalment of € 1.5 million for the Aesthetic and Dental divisions, which were sold last year, and the payment of an outstanding residual purchase price claim by the company Biolase Europe GmbH to the amount of € 1.2 million. Biolase Europe GmbH was obliged to make this payment on the basis of an agreement with the former Asclepion-Meditec AG on the sale of a production facility.

At € 2.9 million the balance sheet items "Loans" was of approximately the same magnitude posted in the previous year (€ 2.8 million). The out-of-court settlement in the lawsuit against I-Spire s.p.r.l., Brussels, Belgium, and its sole shareholder reduced this figure. This settlement foresees the payment of the total amount of € 2.8 million shown in the balance sheet item "Loans" by I-Spire s.p.r.l. in several instalments. In the period under review I-Spire s.p.r.l. paid the first instalment of € 1.5 million. The item was increased by a loan of € 1.6 million to the cooperation partner Notal Vision, Inc. Carl Zeiss Meditec cooperates with Notal Vision, Inc. in the field of the early diagnosis of age-related macular degeneration (AMD).

There were no major changes over the previous year on the liabilities side of the balance sheet. Merely the "Income taxes payable" decreased to € 2.8 million (previous year: € 6.7 million). The reason for this lies in the fact that the Japanese subsidiary Carl Zeiss Meditec Co. Ltd. paid its tax liabilities earlier than it had in the previous year. Due to the successful development of business the "Retained earnings" more than doubled over the previous year. As of 30 September 2004 the latter totalled € 24.6 million compared to € 12.0 million as of 30 September 2003.

Figure 7 summarises the structure of the consolidated balance sheets as of 30 September 2004 and 2003, respectively.

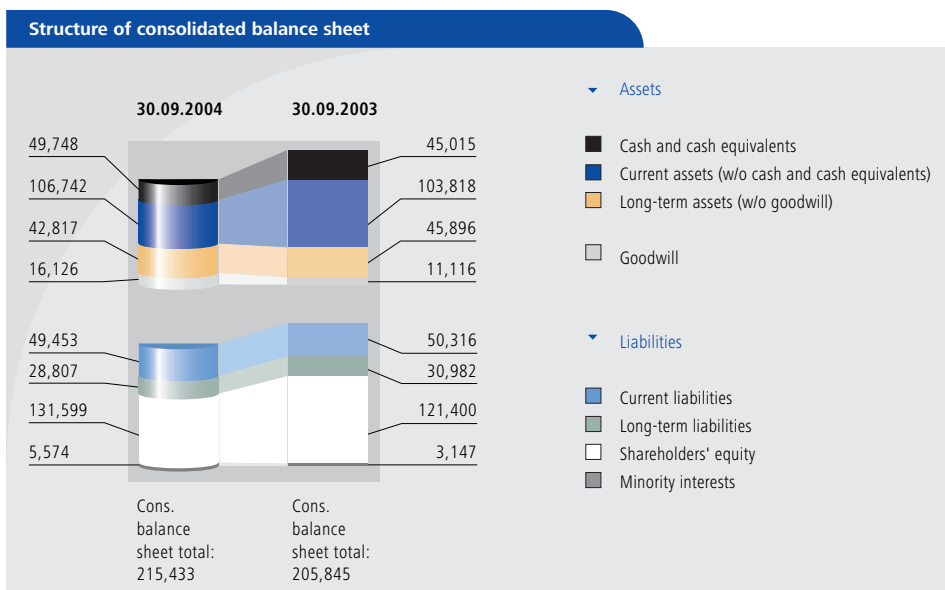


Figure 7:  
Structure of  
consolidated balance sheet  
as of 30 September 2004 and 2003  
(in € '000)

### b) Key ratios relating to net worth

Thanks to the successful development of business the Carl Zeiss Meditec Group was able to further improve its solid balance sheet structure in the period under review. Alongside an increase in the equity ratio and a reduction in the *days of sales outstanding* (DSO) over the previous year, the decrease of 95.2% in the net level of debt over the previous year is of some significance.

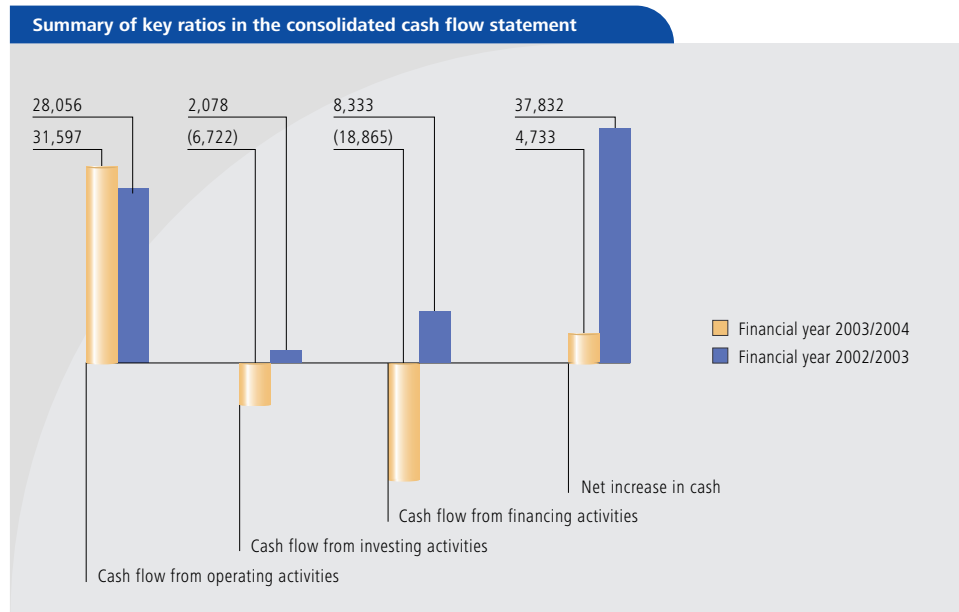
Table 1:   
Key data of net worth  
as of 30 September 2004  
and 2003

| Key ratios                         | Definition   | 30.09.2004                  | 30.09.2003                  | Change                    |
|------------------------------------|--|-----------------------------|-----------------------------|---------------------------|
| Equity ratio                       | Equity capital   | 61.1%                       | 59.0%                       | +2.1<br>percentage points |
|                                    | Balance-sheet total  |                             |                             |                           |
| Net debt                           | Liabilities  | € 1,160,000                 | € 24,194,000                | -95.2%                    |
|                                    | less cash and cash equivalents<br>less accounts receivable from group<br>treasury of the Carl Zeiss AG |                             |                             |                           |
| Net financial debt                 | Interest-bearing liabilities   | € (48,827,000) <sup>7</sup> | € (26,971,000) <sup>7</sup> | +81.0%                    |
|                                    | less cash and cash equivalents<br>less accounts receivable from group<br>treasury of the Carl Zeiss AG |                             |                             |                           |
| Inventory turnover                 | Cost of goods sold   | 3.5                         | 3.4                         |                           |
|                                    | Average on inventories   |                             |                             |                           |
| Days of Sales<br>Outstanding (DSO) | Trade accounts<br>receivable   | 53.3 days                   | 59.1 days                   |                           |
|                                    | Consolidated sales x 360 days  |                             |                             |                           |

## 14. Financial position

### a) Statement of financial position

Figure 8:   
Summary of key ratios  
in the consolidated  
cash flow statement  
  
(in € '000)



In the period under review the Carl Zeiss Meditec Group again succeeded in enhancing its financial strength. Compared to the previous year cash flow from operating activities improved by 12.6%, up from € 28.1 million to € 31.6 million. The following factors were essentially responsible for this:

- active management of the current assets: The further reduction in receivables and the decrease in the inventories improved the operating cash flow.
- the considerable improvement in the consolidated net income: The consolidated net income almost doubled over the financial year 2002/2003. In the reporting period it amounted to € 12.6 million (previous year: € 6.6 million).

Cash flow from investing activities in the financial year 2003/2004 stood at € -6.7 million (previous year: € 2.1 million). The major item in this respect is the acquisition of hiko medical communication GmbH with a volume of € 5.8 million (cf. also Section "12. Events of particular significance"). Investments in property, plant and equipment totalled € 2.8 million, and were thus at about the same level seen in the financial year 2002/2003 (€ 2.8 million). The Capex ratio, i.e. investments as a ratio of consolidated sales, was thus 1.2% (previous year: 1.2%).

In the reporting period the cash flow from financing activities amounted to € -18.9 million (previous year: € 8.3 million). In the financial year 2003/2004 the cash inflows from operating activities were invested with the group treasury of Carl Zeiss AG at the customary market conditions. This is recorded in the cash flow statement under "Increase in receivables due from treasury" and thus has a negative sign. In the previous year the net cash inflow of € 24.3 million essentially resulted from the capital increase at Carl Zeiss Meditec. The total receivables transferred to the group treasury in the period under review were € 15.8 million (previous year: € 5.1 million).

The net increase in cash and cash equivalents in the financial year 2003/2004 amounted to € 4.7 million (previous year: € 37.8 million).

#### **b) Key ratios relating to financial position**

Above all, the reduction in the *net working capital* by 27.7%, from € 41.4 million in the previous year to € 29.9 million as of 30 September 2004, reflects the successes in the optimisation of the inventories and the reduction in accounts receivable and other assets. Accordingly, the increase in the *working capital* ratio over the previous year is solely attributable to the rise in cash and cash equivalents and to the rise in the credit with the group treasury of the Carl Zeiss AG. Coverage of the current liabilities by the current assets has thus further improved.

Table 2: ▶  
Key ratios relating to  
financial position as of  
30 September 2004  
and 2003  
  
(in € '000)

| Key ratios                    | Definition   | 30.09.2004 | 30.09.2003 | Change |
|-------------------------------|--|------------|------------|--------|
| Cash and cash equivalents     | Cash at bank and in hand   | 49,748     | 45,015     | +10.5% |
| Net cash and cash equivalents | Cash at bank and in hand<br>+ accounts receivable<br>from group treasury of<br>the Carl Zeiss AG<br>less accounts payable<br>to group treasury of<br>the Carl Zeiss AG | 77,100     | 57,067     | +35.1% |
| Net working capital           | Current assets<br>less cash and cash<br>equivalents<br>less accounts receivable<br>from group treasury of<br>the Carl Zeiss AG<br>less current liabilities             | 29,937     | 41,413     | -27.7% |
| Working Capital               | Current assets<br>less current liabilities   | 107,037    | 98,517     | +8.6%  |

Table 3: ▶  
Key ratios of  
financial position in the  
financial years 2003/2004  
and 2002/2003  
  
(in € '000)

| Key ratios          | Definition                                 | Financial year 2003/2004 | Financial year 2002/2003 | Change               |
|---------------------|--|--------------------------|--------------------------|----------------------|
| Cash flow per share | Cash flow from operating activities        | € 1.11                   | € 1.08                   | +2.8%                |
|                     | Weighted average of shares outstanding     |                          |                          |                      |
| Capex ratio         | Cash flow from investments in fixed assets | 1.2%                     | 1.2%                     | ±0 percentage points |
|                     | Consolidated sales                         |                          |                          |                      |

## 15. Investing activities

As already seen in Section "14. Financial position, a) Statement of financial position", the acquisition of hiko medical communication GmbH was the most significant investment by the Group in the period under review. Investments in property, plant and equipment totalled € 2.8 million, and were thus at about the same level seen in the financial year 2002/2003.

## 16. Earnings position

### a) Statement of earnings

| Key ratios                                | Financial year 2003/2004 | Financial year 2002/2003 | Change over previous year |
|---|--------------------------|--------------------------|---------------------------|
| Sales                                     | 234,878                  | 235,714                  | -0.4%                     |
| Gross margin                              | 46.4%                    | 43.5%                    | +2.9 percentage points    |
| Earnings before interest and taxes (EBIT) | 26,326                   | 24,723                   | +6.5%                     |
| EBIT margin                               | 11.2%                    | 10.5%                    | +0.7 percentage points    |
| Consolidated net income                   | 12,610                   | 6,558                    | +92.3%                    |
| Earnings per share (in €)                 | 0.44                     | 0.25                     | +76.0%                    |

Table 4:  
Summary of key ratios  
in the consolidated income statement  
for the financial years 2003/2004  
and 2002/2003

(in € '000)

At € 234.9 million the consolidated sales in the financial year 2003/2004 were at about the same level seen in the previous year (€ 235.7 million). In the fourth quarter the Carl Zeiss Meditec Group posted sales of € 64.5 million, a much higher figure than that seen in the preceding quarters. Viewed over the course of the whole year the considerable decrease in the value of the US dollar over the euro, and thus the corresponding negative impact on the conversion of the consolidated sales from US dollars into euros, was virtually compensated for. Figure 9 provides an overview of the quarterly sales development.

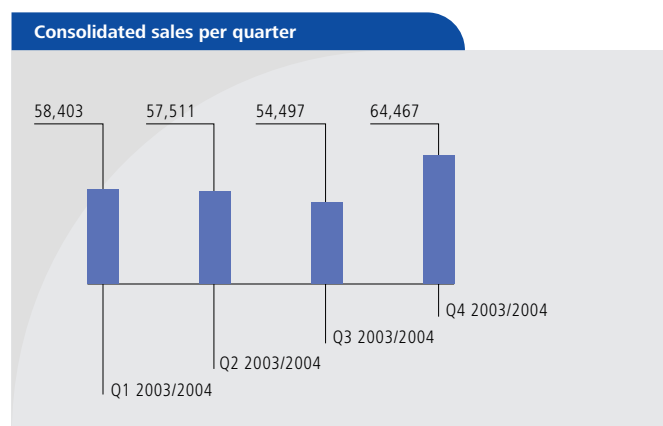


Figure 9:  
Consolidated sales per quarter  
in the financial year 2003/2004

(in € '000)

There was a significant improvement in the Group's gross margin compared to the previous year. In the financial year 2003/2004 it amounted to 46.4% following on from 43.5% in 2002/2003. This represents an increase of 2.9 percentage points. The reasons for this development are:

- Further optimisation of the cost of goods sold: It was possible to make further progress in this area, in particular thanks to the process optimisations and improvements in the field of "Procurement".
- Change in product mix: The proportion of innovative and powerful diagnosis and therapy systems in the consolidated sales increased in the period under review.

The function costs increased to € 83.7 million, following from € 77.6 million in the previous year. This development has arisen as follows:

- In comparison to the financial year 2002/2003 the selling and marketing expenses rose by 8.2% to € 47.1 million (previous year: € 43.6 million). This is due, among other things, to the development of additional sales capacities in the USA. Thus not only has it been possible to compensate for the loss of the low-margin OEM sales, which were suspended as of the beginning of the financial year, but also to attain a clear increase in sales in the local currency (cf. also Section "3. Development of sales"). Moreover, the marketing activities in the individual markets and for specific products have been extended. A further increase in the costs in this area over the previous year results from the fact that the Japanese subsidiary Carl Zeiss Meditec Co. Ltd. was only consolidated for 11 months in the previous year, yet the corresponding costs are included in full for the period under review. The marketing and selling cost ratio thus amounted to 20.1% of consolidated sales (previous year: 18.5%).
- The increase in administrative costs is mainly due to the formation of provisions for two pending litigations (cf. also Risk Report, Section "11. Legal risks"), as well as a change in allocation of costs for the quality management of Carl Zeiss Meditec AG, Jena, over the previous year. Half of these costs are now stated under "General and administrative expenses", the other half under "Cost of goods sold" (in previous year: fully allocated to "Cost of goods sold"). Furthermore, Carl Zeiss Meditec, Inc., Dublin, incurred higher personnel costs due to the successful business development. Relative to consolidated sales the administrative expenses ratio rose to 5.0% in the financial year 2003/2004 (previous year: 4.7%).
- In the financial year 2003/2004 the Group spent € 24.9 million on research and development (previous year: € 22.9 million). Granted subsidies of € 1.0 million (previous year: € 1.8 million) are included in this amount. Relative to consolidated sales the research and development costs ratio increased to 10.6% in the financial year 2003/2004, following on from 9.7% in the previous year. The main reasons for this are the development of additional capacities in this area at Carl Zeiss Meditec, Inc., as well as costs incurred in connection with approvals for products in the USA. Among these are, for example, the MEL 80™ and the PreviewPHPTM system.

On the basis of the development of operating activities within the Group, earnings before interest and tax (EBIT) improved by 6.5% to € 26.3 million (previous year: € 24.7 million). The EBIT margin increased by 0.7 percentage points to 11.2% (previous year: 10.5%).

Earnings before tax (EBT) also increased significantly compared to the previous year. They amounted to € 25.1 million (previous year: € 22.6 million). In addition to the positive trend in the operating business, this was also attributable to the substantial decrease in interest expenses. These fell from € 2.1 million in the previous year to € 1.2 million in the financial year 2003/2004.

The tax ratio decreased to 39.1% in the financial year 2003/2004, following on from 39.8% in the previous year.

In total Carl Zeiss Meditec posted a consolidated net income of € 12.6 million, following on from € 6.6 million in the previous year. This represents an increase of 92.3%. Accordingly the earnings per share improved to € 0.44 (previous year: € 0.25) despite the increase in the weighted average number of shares outstanding to 28.4 million (previous year: 25.9 million).

### b) Key ratios relating to earnings position

The key ratios relating to the earnings position confirm the successful development of business for the Carl Zeiss Meditec Group. Above all the growth in the return on equity and the return on assets show that the deployment of the necessary resources for the business operation has been further optimised. Figure 10 shows the development of key ratios in a year-on-year comparison.

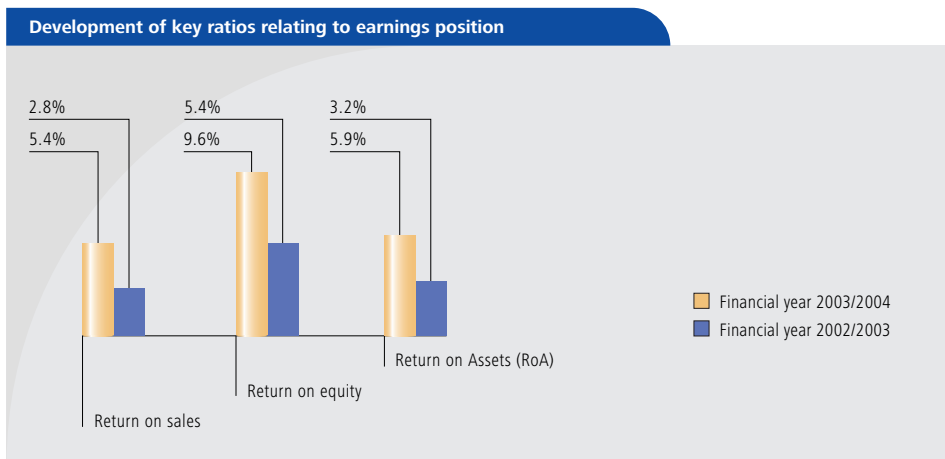


Figure 10: Development of key ratios relating to earnings position in the financial years 2003/2004 and 2002/2003

## Risk report

### 1. Risk management system

In the course of its business, the Carl Zeiss Meditec Group is naturally exposed to a number of risks that are inherent to commercial activities.

Risk management at Carl Zeiss Meditec is an integral part of corporate management and is based on three major components:

- Risk management system: In order to be able to identify and assess risks in good time and take the appropriate steps, the Group has introduced a risk management system. An important element is a database-aided software solution with which risks and their estimated probability of occurrence and potential for damage may be recorded, systematised and evaluated on a regular basis. The Group thus satisfies the legal requirements with regard to control and transparency (KonTraG, Act on Control and Transparency in Stock Corporations).
- Controlling instruments: Controlling at Carl Zeiss Meditec regularly informs the Management Board, the Managing Directors of the subsidiaries and all responsible decision-makers within the Carl Zeiss Meditec Group in a timely manner on emerging risks on the basis of key ratios, thereby supplementing the risk management system.
- Certified quality management: A further critical component is the Group's certified quality management (see also: Business Report, Section "8. Quality management"). Clearly structured and documented processes within the framework of quality management ensure not only transparency – in most markets they are a prerequisite for the sale of medical products in the meantime. The quality assurance system employed by Carl Zeiss Meditec was certified by DQS GmbH Deutsche Gesellschaft zur Zertifizierung von Managementsystemen and conforms to the US standard for "Good Manufacturing Practice" (GMP), 21 C.F.R. part 820, QSR. A major objective of this certified process is risk avoidance.

The risk management system is an integral part of the overall controlling and reporting process of the Group and ensures the systematic recording and evaluation of risks. Furthermore, it guarantees that relevant information is forwarded without delay to the Group's decision-makers.

The main features of this system are:

- Under the direction of a central risk manager, the responsible staff on the different sites regularly examine processes, transactions and developments for existing risks.
- Risk identification and evaluation using standardised risk matrices.
- Regular risk reports are sent to the Management Board, the Managing Directors of the subsidiaries and other decision-makers within the Group on the basis of given threshold values for relevant risks and according to the classification using the risk matrices.
- On this basis suitable steps are taken to avoid identified risks, reduce the likelihood of such risks occurring or minimise the financial losses incurred.

As with the internal reporting, the risk management system is subjected to an internal audit. In addition the audit formed a constituent part of the annual audit by the certified auditor.

## **2. Market and competition**

The competition on the medical technology market in general and in ophthalmology in particular will continue to increase. Fundamentally there is the risk that, compared to competitors, Carl Zeiss Meditec might not react in good time to market developments with new products and adaptations of existing products. Such an event would have negative consequences for the net worth, financial position and earnings, and also lead to a deterioration of the market position.

Carl Zeiss Meditec actively counters this risk by making not inconsiderable investments in the field of research and development, and also in the upstream areas Market Intelligence, New Business Development and Advanced Technologies.

Furthermore, government reforms in the social system could have a negative effect on the Group's sales volume and earnings situation. This risk exists particularly in countries in which a major portion of treatments for eye ailments is paid by health insurance schemes. If budgets were cut, or the reimbursement of treatment costs were denied for certain types of treatment, this could have a negative impact on the Group's net worth, financial position and earnings.

An additional risk potential exists in a possible further deterioration in the economic situation, and in particular with respect to the markets that are critical to the Group. This could have a marked effect on privately financed medical applications such as refractive surgery: In this case there is a risk of deterioration in the financial standing of the Group's customers or the demand for its products. Due to a loss of sales and receivables this could have a negative impact on the net worth, financial position and earnings of Carl Zeiss Meditec.

### **3. New technology and products**

Medical technology as a whole, particularly in the field of ophthalmology, is undergoing an extremely dynamic development process. New scientific findings lead to shorter development and product cycles. Such findings may have a negative impact on existing methods and products and also on new methods and products on which the business success of the Group is founded.

The success of the Carl Zeiss Meditec Group is determined to a great extent by the development of innovative products in the fields of ophthalmology and by recognising new technology trends at an early stage and turning these into the appropriate products. Should the Group lose touch in technological terms, fail to react in time to a technological development, not identify a market trend in good time or should a development end in a technological dead-end, this could have a negative impact on the competitive position of the Group.

Carl Zeiss Meditec is actively countering this risk, however, with the measures shown in Section "2. Market and competition".

### **4. Approval of products**

In the medical technology and the health service sectors there are strict approval procedures that vary from one country to another. Denial of or delays in approval procedures for the Group's products could have a negative impact on the future sales and profits of the Carl Zeiss Meditec Group.

There is no guarantee that the Group's numerous approvals will continue to be valid in the future, renewed or obtained in good time so as to launch new new products ahead of its competitors. Furthermore, stricter approval requirements must be reckoned with in future. This would have negative consequences for the net worth, financial position and earnings of Carl Zeiss Meditec.

In order to identify such developments in good time and be able to react appropriately, the Group follows developments in this field extremely closely, monitoring the details of approval procedures within the framework of its implemented quality management system.

## **5. Dependence on suppliers**

The increasingly close cooperation with suppliers necessitated by the general cost pressure and complexity of the supplied components implies a greater dependence on one another. This could have negative implications for the production, sales and the quality of the Group's products.

Thanks to the qualification of its suppliers, the identification of secondary suppliers and the preparation of a strategic inventory plan, Carl Zeiss Meditec takes the best-possible measures to counter this risk.

## **6. Patents and intellectual property**

The Carl Zeiss Meditec Group is not aware of any material violation of patent rights or other industrial property rights of third parties. The possibility that a third party may assert claims against the Group for the violation of industrial property rights cannot, however, be ruled out. A violation of this type could result in a delay in the delivery of products. In the event of a negative outcome of the proceeding, the Group may be obliged to enter into fee or licensing arrangements. There is a risk that such copyright or licensing agreements are not available or only available on unacceptable terms. A lawsuit against Carl Zeiss Meditec AG or one of its subsidiaries due to the violation of industrial property rights could therefore have a negative impact on the net worth, financial situation and earnings of the Group.

The competitive position of the Carl Zeiss Meditec Group depends on securing its technological innovations. So as to guarantee these, the Group acquires patents for its own and third-party inventions and takes measures to protect its business secrets. The expiry of industrial property rights or patents could result in the emergence of new competitors on the market or strengthen the position of competitors who are already active.

In order to avoid the above-mentioned legal disputes, patents and patent applications in the relevant fields are analysed by the Group at regular intervals.

## **7. Protection against loss of confidential data**

In the sphere of IT solutions the Group has established a number of mechanisms for the protection of confidential data. Nevertheless, breaches of security and the loss of this data cannot be completely ruled out. This could have an adverse effect on the competitive position of the Group.

## **8. Product liability risk**

In some of the Group's products employed for medical treatments there is an inherent fundamental risk that malfunctions result in injury to the patient. Despite employing all reasonable quality control measures and complying with all legal provisions, this risk cannot be completely excluded. Although the Carl Zeiss Meditec Group has to date not been obliged to pay any major claims for compensation arising from product liability, no guarantee can be given that the Carl Zeiss Meditec Group will not be confronted with such claims in the future.

The Group has covered itself against possible product liability claims by means of product liability insurance. A particular risk is posed by potential product liability claims brought against the Group in the USA as the damages awarded by the courts there may be very large indeed. It cannot be completely excluded that the Group's existing insurance cover does not provide sufficient cover for potential claims in the USA.

## **9. Subsidiaries**

The Carl Zeiss Meditec Group is indirectly exposed to the risk environment of each of its subsidiaries. The relationship to its subsidiaries can result in statutory and contractual liabilities.

## 10. Goodwill

The goodwill stated on the consolidated balance sheet, resulting from the acquisition of the former Asclepion-Meditec AG by Carl Zeiss Ophthalmic Systems AG and the take-over of the former hiko medical communication GmbH, is not amortised on a scheduled basis but, in accordance with SFAS 142 is regularly examined vis-à-vis its value within the framework of annual impairment tests. An impairment test performed in the reporting period produced the full value of assets recognised in this balance sheet item. On the basis of business trends, the Group anticipates positive results for future tests. However, there is still a risk of a long-term deterioration in the net worth, financial position and earnings, with the attendant consequences for the amount of goodwill to be shown in the balance sheet.

## 11. Legal risks

The Group has reached an out-of-court settlement in the action for damages against I-Spire s.p.r.l., Brussels/Belgium and its sole proprietor. Inasmuch, any possible risks may be considered as having been eliminated to the greatest-possible degree. The settlement includes payments of the total amount of € 2.8 million shown in the balance sheet item "Other loans" by I-Spire s.p.r.l. in several instalments. The payment of the first two instalments totalling € 1.8 million were recorded at the end of April and after the balance sheet cut-off date in October 2004.

Current litigation risks arise from the lawsuit and claim for lost earnings filed by a distributor of the former Asclepion for dermatological lasers, and the pending cost reimbursement lawsuit and claim filed by the insolvency administrator of the former Asclepion distribution partner U.S. Medical, Inc., also in the field of dermatological lasers. The Company has, from today's stance, taken adequate precautionary measures in the form of provisions.

## Research and development report

### 1. General comments

In the financial year 2003/2004 Carl Zeiss Meditec spent € 24.9 million on research and development (R&D) (previous year: € 22.9 million). A total of € 1.0 million was granted in subsidies (previous year: € 1.8 million). Relative to the consolidated sales the R&D ratio increased in the period under review from 9.7% in the previous year to 10.6%. The reason for this development was, above all, the expansion of additional R&D capacities at the American company Carl Zeiss Meditec, Inc., as well as costs incurred in connection with approvals for products in the USA. Among these approvals are those for the MEL 80™ and the PreviewPHP™ system. This further focus on research and development is clear evidence of its importance in securing the future growth of the Group.

As of 30 September 2004 162 staff within the Group were employed in R&D (previous year: 143); this corresponds to 20.4% of the total workforce (previous year: 19.0%).

### 2. Projects

A number of significant R&D projects were successfully concluded in the reporting period with the market launch of the corresponding products. These included the two software products GPA™ and VISUPAC™ 4.0, as well as new software upgrades for the STRATUSocT™ system, the diagnostic system PreviewPHP™ and the ACMaster™ (cf. also Section "3. New Products in the financial year 2003/2004").

Major R&D projects at group level concern the further expansion of the range of applications and functionality of products already successfully launched on the market. Among these are the systems STRATUSocT™ and HFA II*j*, as well as the refractive laser MEL 80™ and the CRS Master™. Further projects in the sphere of research and development are concerned with the continued or new development of innovative perimetric systems, digital fundus cameras and the optimisation of the product portfolio in the field of ophthalmic lasers.

In addition, the fundamentals and outlook for future diagnostic and therapy systems were examined in other group projects. Above all, systems which allow for an increase in efficiency for physicians and improved diagnostic and treatment results for patients will be of even greater significance on the market in the future in the view of the Group. The Group assumes that in the future physicians, patients, health policy and health insurance companies will focus to a greater degree on the early detection and treatment of serious eye diseases – for instance glaucoma and various retinal diseases.

Together with the American company Calhoun Vision, Inc., Carl Zeiss Meditec has been working on the development of a new type of intraocular lens whose refractive power can be adjusted after the operation without the need for further surgical intervention. In this way, cataract surgery can be coupled with the optimum customised correction of vision defects. The digital light source required for the purpose is being developed by Carl Zeiss Meditec, the respective lens by Calhoun Vision, Inc.

Further activities in the field of research and development concerned the processes for the US approval of new products such as the MEL 80™ and the PreviewPHP™

### 3. New products in the financial year 2003/2004

In the financial year 2003/2004 the following products were brought onto the market by Carl Zeiss Meditec Group:

- **Glaucoma Progression Analysis™ Software (GPA™):** This is software for the management of glaucoma with the aid of the HFA IIi system.
- **VISUPAC™ 4.0:** With VISUPAC™ 4.0 it is possible to intelligently combine different diagnostic systems, such as fundus cameras and the STRATUSoc™ system, and, moreover, to link these up to practice management and hospital information systems.
- **Software 4.0 for the STRATUSoc™ system:** This software upgrade expands the functionality and heightens the operating comfort of the diagnostic system STRATUSoc™.
- **PreView PHP™:** The PreviewPHP™ diagnostic system represents a new approach to the early detection and monitoring of age-related macular degeneration (AMD), a serious retinal disorder.
- **ACMaster™:** With the AC Master™, which just like the IOL Master® is based on optical biometry, the front section of the eye may be examined with the greatest precision, something which is of significance above all in connection with the use of innovative intraocular lenses.
- **VISULAS™ YAG III:** This laser system will be deployed in the follow-up treatment of cataract operations.

## Supplementary report

On 21 October 2004 the Carl Zeiss Meditec Group announced that it intends to take over the American company Laser Diagnostic Technologies, Inc. (LDT) domiciled in San Diego, California, USA, through Carl Zeiss Meditec, Inc.. LDT developed and commercialised a new standard for glaucoma detection with its proprietary ocular nerve fiber measurement instrument. For the current financial year 2004 LDT expects sales of some US \$ 20 million and a balanced operating result. Carl Zeiss Meditec assumes that the transaction can be concluded by the end of 2004 following the necessary approvals from the corresponding executive bodies and shareholders of LDT.

LDT's main product, the GDx VCC, is a system specially developed for the early detection and diagnosis of glaucoma. It thus complements the market presence of Carl Zeiss Meditec's STRATUSocT™, a retinal imaging system with a wide range of possible applications. These include not only the early detection of glaucoma, but also its use in the diagnosis of other severe eye ailments such as age-related macular degeneration (AMD), in diabetic retinopathy, as well as in examinations before and after the treatment of cataracts. In this manner, the system GDx VCC is primarily aimed at customers who do not require the full bandwidth of examination possibilities, such as is offered by the system STRATUSocT™.

On 1 November 2004 Carl Zeiss Meditec also announced that its Japanese subsidiary, Carl Zeiss Meditec Co., Ltd., domiciled in Tokyo, Japan, was taking over the surgery business of Carl Zeiss Co., Ltd. which is also domiciled in Tokyo, Japan. This business is concerned with the sale of surgical microscopes for ophthalmology, neurosurgery and for ear, nose and throat surgery, and has annual sales of ca. € 25 million. In the opinion of the Carl Zeiss Meditec Group this move allows for the realisation of considerable synergy effects in various areas such as administration, sales administration, and service. Moreover, in this manner the subsidiary can reinforce and better coordinate its activities regarding approvals issues.

## Forecast

### 1. Economic conditions

For 2005 Germany's economic research institute Deutsches Institut für Wirtschaftsforschung ("DIW") expects a further increase in overall economic output in the industrialised nations. If the favourable monetary framework conditions, such as low interest rates for loans, are kept in place, this should also have a favourable impact on further investment. From the stance of DIW the economic dynamism in East Asia and in those threshold countries which export raw materials will remain high in 2005 despite a slight downturn.<sup>8</sup> "On the whole the driving forces behind the economy seem to be so stable that, despite the rise in oil prices and the waning stimulus from monetary and financial policy, a drift towards a downturn is not to be expected."<sup>9</sup>

For the USA and Japan a downturn in the gross domestic product ("GDP") is expected for 2005. For the USA an improvement of 3.4% (2004: 4.4%) is expected in the GDP in 2004; in Japan the figure is set to be 2.1% (2004: 4.2%). The economic expectations of DIW for these economic regions are still higher than those for the euro-zone; here growth of 2.0% has been forecast for the GDP.<sup>10</sup> For Germany DIW assumes that there will only be a mild recovery in private consumption in 2005. However, DIW is also of the opinion that the readiness to invest will pick up slightly in 2005. One of the reasons seen for this is the ongoing expansion of capacities, which would make replacement and expansion investment necessary. Seen as a whole, however, the export sector will once again be the driving force behind German industry.<sup>11</sup>

### 2. Outlook

In the financial year 2003/2004 Carl Zeiss Meditec fulfilled important internal prerequisites for a future acceleration of growth. Alongside an extensive improvement in the net worth, financial and earnings position in the period under review, progress was also made in further improving the efficiency of internal process flows.

Once again the Group reasserts its target of doubling its sales revenue by the end of the 2007/2008 financial year.<sup>12</sup> The earnings power is to be reinforced continually and on a sustainable basis at the gross margin and EBIT margin level, as is the return on sales. In the financial year 2007/2008 the gross margin is to be around 50%. The EBIT margin is then set to be some 15%. To this end, the product portfolio is to be extended through the inclusion of innovative systems, and existing resources deployed even more efficiently.

<sup>8</sup> Cf. *ibid.*, p. 633

<sup>9</sup> *Ibid.* p. 633

<sup>10</sup> Cf. *ibid.*, p. 630-644

<sup>11</sup> Cf. *ibid.*, p. 645-663

<sup>12</sup> Reference: consolidated sales in the financial year 2002/2003

### 3. Strategy

Based on the excellent position of the Group with devices and systems for ophthalmology, Carl Zeiss Meditec intends to establish itself as a provider of complete solutions in this field. To this end the existing competitive position in the field of the four main ophthalmic disorders is to be enhanced. The unique technology and product portfolio, the extensive expertise in the field of research and development, the strong global marketing network and the world-famous brand name "Zeiss" provide an excellent basis for this. The acquisition of the American company Laser Diagnostic Technologies, Inc., which was announced at the end of October 2004, is further testimony to the fact that wherever it makes sense external growth options can also be utilised.

Jena, 22 November 2004



**Ulrich Krauss**  
*President and CEO*



**Bernd Hirsch**  
*Member of the  
Management Board*

## Consolidated income statement

| € '000  | Notes     | Financial year 2003/2004 | Financial year 2002/2003 |
|---|-----------|--------------------------|--------------------------|
| Sales   | (2o) (23) | 234,878                  | 235,714                  |
| Costs of goods sold   | (2q)      | (125,877)                | (133,184)                |
| Gross profit  |           | 109,001                  | 102,530                  |
| Selling and marketing expenses  |           | (47,123)                 | (43,563)                 |
| General and administrative expenses                                       |           | (11,699)                 | (11,112)                 |
| Research and development expenses   |           | (25,874)                 | (24,688)                 |
| minus government grants received  | (2u) (15) | 977                      | 1,790                    |
| Other operating income / (expense), net                                   |           | 252                      | 519                      |
| Foreign currency gains / (losses)   | (2b) (2l) | 792                      | (753)                    |
| Earnings before interest result and taxes                                 |           | 26,326                   | 24,723                   |
| Interest income / (expense), net  |           | (1,164)                  | (2,075)                  |
| Appreciation, depreciation and valuation adjustments on financial assets  |           | (69)                     | -                        |
| Earnings before tax   |           | 25,093                   | 22,648                   |
| Income tax expense from continuing operations                             | (22)      | (9,812)                  | (9,014)                  |
| Minority interests  | (21)      | (2,671)                  | (2,880)                  |
| Net income from continuing operations                                     |           | 12,610                   | 10,754                   |
| Income / (loss) before income taxes from discontinued operations*         |           | -                        | (5,934)                  |
| Income tax benefit from discontinued operations                           |           | -                        | 1,738                    |
| Net income from discontinued operations                                   |           | -                        | (4,196)                  |
| Net income  |           | 12,610                   | 6,558                    |
| Earnings per share, basic (€)   | (2s)      |                          |                          |
| From continuing operations  |           | 0.44                     | 0.41                     |
| From discontinued operations  |           | -                        | (0.16)                   |
| Total   |           | 0.44                     | 0.25                     |
| Earnings per share, diluted (€)   | (2s)      |                          |                          |
| From continuing operations  |           | 0.44                     | 0.41                     |
| From discontinued operations  |           | -                        | (0.16)                   |
| Total   |           | 0.44                     | 0.25                     |
| Weighted average number of shares outstanding for the period under review |           |                          |                          |
| Basic   |           | 28,402,339               | 25,918,166               |
| Diluted   |           | 28,402,339               | 25,918,166               |

\*These allow for a loss of € 4.5 million on the sale in the previous year.  
The following notes to the consolidated financial statements are part of the consolidated financial statements.

## Consolidated balance sheet

| €'000  | Notes        | 30.09.2004     | 30.09.2003     |
|--|--------------|----------------|----------------|
| Assets   |              |                |                |
| Current assets:  |              |                |                |
| Cash   | (2d)         | 49,748         | 45,015         |
| Restricted Cash  | (2d)         | -              | 850            |
| Trade accounts receivable, net of allowances of<br>€ 12.032m (prev. year: € 10.478m)         | (2e) (5)     | 26,243         | 30,344         |
| Accounts receivable from affiliated companies  | (4)          | 35,915         | 20,451         |
| Inventories  | (2f) (7)     | 34,126         | 38,611         |
| Prepaid expenses   |              | 1,831          | 1,132          |
| Deferred income taxes  | (2n) (22)    | 7,419          | 7,958          |
| Other assets   | (6)          | 1,208          | 4,472          |
| <b>Total current assets</b>  |              | <b>156,490</b> | <b>148,833</b> |
| Property, plant, and equipment, net  | (2g) (8)     | 24,070         | 26,000         |
| Goodwill   | (2h) (3) (9) | 16,126         | 11,116         |
| Other intangible assets, net   | (2i)         | 5,383          | 5,079          |
| Other long-term accounts receivable, net of allowances of<br>€ 0.012m (prev. year: € 0.047m) | (5)          | 393            | 718            |
| Loans  | (10)         | 2,871          | 2,818          |
| Deferred income taxes  | (2n) (22)    | 10,068         | 11,281         |
| Other non-current assets   |              | 32             | -              |
| <b>Total assets</b>  |              | <b>215,433</b> | <b>205,845</b> |

The following notes to the consolidated financial statements are part of the consolidated financial statements.

| €'000   | Notes     | 30.09.2004     | 30.09.2003     |
|---|-----------|----------------|----------------|
| Liabilities and shareholders' equity                                |           |                |                |
| Current liabilities:  |           |                |                |
| Current portion of long-term debt                                   | (14)      | 198            | 187            |
| Current portion of capital lease obligations                        | (17)      | 656            | 374            |
| Trade accounts payable  |           | 10,592         | 10,636         |
| Accounts payable to affiliated companies                            | (4)       | 5,072          | 5,919          |
| Income taxes payable  |           | 2,779          | 6,655          |
| Deferred income   |           | 4,670          | 4,870          |
| Deferred income taxes   | (2n) (22) | 108            | 8              |
| Provisions  | (11) (13) | 23,431         | 20,527         |
| Other current liabilities   | (12)      | 1,947          | 1,140          |
| <b>Total current liabilities</b>                                    |           | <b>49,453</b>  | <b>50,316</b>  |
| Long-term debt, net of current portion                              | (14)      | 4,644          | 4,841          |
| Capital lease obligations, less current portion                     | (17)      | 22,775         | 24,731         |
| Long-term deferred income   |           | 682            | 1,007          |
| Deferred income taxes   | (2n) (22) | 563            | 226            |
| Other liabilities   |           | 143            | 177            |
| <b>Total liabilities</b>  |           | <b>78,260</b>  | <b>81,298</b>  |
| Minority interests  | (21)      | 5,574          | 3,147          |
| Shareholders' equity:   |           |                |                |
| 28,416,629 ordinary shares with an imputed nominal value of € 1.00, | (20)      | 28,417         | 28,417         |
| Additional paid-in capital  | (20)      | 89,433         | 89,433         |
| Retained earnings   | (20)      | 24,642         | 12,032         |
| Accumulated other comprehensive loss                                | (2r) (20) | (10,715)       | (8,374)        |
| Treasury stock  | (20)      | (178)          | (108)          |
| <b>Total shareholders' equity</b>                                   |           | <b>131,599</b> | <b>121,400</b> |
| <b>Total liabilities and shareholders' equity</b>                   |           | <b>215,433</b> | <b>205,845</b> |

The following notes to the consolidated financial statements are part of the consolidated financial statements.

## Consolidated cash flow statement

| € '000  | Financial year 2003/2004 | Financial year 2002/2003 |
|---|--------------------------|--------------------------|
| Cash flow from operating activities:  |                          |                          |
| Net income  | 12,610                   | 6,558                    |
| Adjustments to reconcile net income to net cash provided by / (used in) operating activities  |                          |                          |
| Minority interest   | 2,671                    | 2,880                    |
| Depreciation and amortisation   | 5,405                    | 5,775                    |
| Amortisation of financial assets  | 69                       | -                        |
| Income from accumulation of interest free receivables   |                          | (125)                    |
| Loss on disposal of fixed assets  | 121                      | 216                      |
| Loss on disposal of discontinued operations   | -                        | 4,500                    |
| Deferred income taxes in connection with the capital increase   | -                        | 281                      |
| Deferred taxes  | 1,304                    | (2,409)                  |
| Change in working capital:  |                          |                          |
| Trade accounts receivable   | 3,156                    | 10,385                   |
| Inventories   | 4,846                    | (5,059)                  |
| Prepaid expenses and other current assets   | 862                      | 1,585                    |
| Trade accounts payable  | 648                      | 2,360                    |
| Accrued tax expenses  | (3,659)                  | 6,518                    |
| Other accrued expenses and liabilities  | 3,811                    | (5,868)                  |
| Deferred income   | (247)                    | 459                      |
| <b>Total adjustments</b>  | <b>18,987</b>            | <b>21,498</b>            |
| <b>Net cash provided by operating activities</b>  | <b>31,597</b>            | <b>28,056</b>            |
| Cash flow from investing activities:  |                          |                          |
| Change of restricted cash   | 850                      | (850)                    |
| Purchase of fixed assets  | (2,825)                  | (2,790)                  |
| Purchase of intangible assets   | (579)                    | -                        |
| Gain on sale of fixed assets  | 83                       | 146                      |
| Payment of loans and investments  | 1,500                    | 2,310                    |
| Cash outflow from the issuing of loans  | (1,646)                  | -                        |
| Inpayment due to the sale of a subsidiary in the context of an asset deal   | -                        | 200                      |
| Inpayment due to the disposal of discontinued operations  | 1,665                    | 1,365                    |
| Acquisition of consolidated companies, net of funds received<br>(Carl Zeiss Meditec Systems GmbH: € 5.770m, Carl Zeiss Meditec Co. Ltd., Tokyo: € 1.697m) | (5,770)                  | 1,697                    |
| <b>Net cash (used in) / provided by investing activities</b>  | <b>(6,722)</b>           | <b>2,078</b>             |
| Cash flow from financing activities:  |                          |                          |
| Repayments of short-term debt   | (1,735)                  | (1,368)                  |
| Repayments of long-term debt  | (415)                    | (178)                    |
| Inpayments from taking up loans from related parties  | (524)                    | 796                      |
| Increase / (decrease) in accounts receivable due to Treasury  | -                        | (9,785)                  |
| (Increase) / decrease in liabilities from Treasury  | (15,762)                 | (5,134)                  |
| Repayments under capital lease contracts  | (359)                    | (347)                    |
| Inpayments due to sale and lease-back transactions  | -                        | 110                      |
| Proceeds from capital increase (net)  | -                        | 24,347                   |
| Purchase of treasury stock  | (70)                     | (108)                    |
| <b>Net cash provided by / (used in) financing activities</b>  | <b>(18,865)</b>          | <b>8,333</b>             |
| Effect of exchange rate changes on liquid assets  | (1,277)                  | (635)                    |
| <b>Net increase in cash</b>   | <b>4,733</b>             | <b>37,832</b>            |
| Cash, beginning of the reporting period   | 45,015                   | 7,183                    |
| <b>Cash, end of the reporting period</b>  | <b>49,748</b>            | <b>45,015</b>            |
| Supplemental disclosures concerning the cash flow:  |                          |                          |
| Interest paid   | 2,187                    | 2,676                    |
| Income taxes paid   | 11,622                   | 4,175                    |

The following notes to the consolidated financial statements are part of the consolidated financial statements.

## Consolidated statement of changes in shareholders' equity

€ '000

|  | Share capital | Additional paid-in capital | Retained earnings | Accumulated other comprehensive loss | Treasury stock | Total shareholders' equity |
|--|---------------|----------------------------|-------------------|--------------------------------------|----------------|----------------------------|
| <i>As per 30.09.2002</i>   | 25,833        | 67,389                     | 5,474             | (3,367)                              | -              | 95,329                     |
| Net income   | -             | -                          | 6,558             | -                                    | -              | 6,558                      |
| Other comprehensive loss (due to currency conversions)                             | -             | -                          | -                 | (5,007)                              | -              | (5,007)                    |
| Accumulated comprehensive income   | -             | -                          | -                 | -                                    | -              | 1,551                      |
| Purchase of treasury stock   | -             | -                          | -                 | -                                    | (108)          | (108)                      |
| Capital increase   | 2,584         | 22,044                     | -                 | -                                    | -              | 24,628                     |
| <i>As per 30.09.2003</i>   | 28,417        | 89,433                     | 12,032            | (8,374)                              | (108)          | 121,400                    |
| Net income   | -             | -                          | 12,610            | -                                    | -              | 12,610                     |
| Other comprehensive loss (due to adjustments of accruals for pensions after taxes) | -             | -                          | -                 | (270)                                | -              | (270)                      |
| Other comprehensive loss (due to currency conversions)                             | -             | -                          | -                 | (2,071)                              | -              | (2,071)                    |
| Accumulated comprehensive income   | -             | -                          | -                 | -                                    | -              | 10,269                     |
| Purchase of treasury stock   | -             | -                          | -                 | -                                    | (70)           | (70)                       |
| <i>As per 30.09.2004</i>   | 28,417        | 89,433                     | 24,642            | (10,715)                             | (178)          | 131,599                    |

The following notes to the consolidated financial statements are part of the consolidated financial statements.

## Development of consolidated fixed assets

### Financial year 2003/2004 (US GAAP)

|   | Costs of purchase / conversion |            |                          |           |           |           | 30.09.2004 |                         |
|---|--------------------------------|------------|--------------------------|-----------|-----------|-----------|------------|-------------------------|
|   | € '000                         | 01.10.2003 | Additions<br>Acquisition | Additions | Transfers | Disposals |            | Currency<br>adjustments |
| Intangible assets and goodwill                                    |                                |            |                          |           |           |           |            |                         |
| Goodwill  |                                | 13,050     | 5,049                    | -         | -         | -         | (141)      | 17,958                  |
| Software  |                                | 444        | 1,318                    | 19        | 125       | (16)      | -          | 1,890                   |
| Other intangible assets   |                                | 6,733      | 21                       | 560       | 155       | (287)     | -          | 7,182                   |
|   |                                | 20,227     | 6,388                    | 579       | 280       | (303)     | (141)      | 27,030                  |
| Property, plant and equipment                                     |                                |            |                          |           |           |           |            |                         |
| Land, buildings and leasehold improvement                         |                                | 27,223     | -                        | 15        | -         | (14)      | (1,107)    | 26,117                  |
| Plant and machinery   |                                | 8,269      | -                        | 103       | 392       | (146)     | (433)      | 8,185                   |
| Other fixtures and fittings, tools and equipment                  |                                | 11,665     | 194                      | 1,194     | 999       | (1,293)   | (332)      | 12,427                  |
| Payments on account and tangible assets in course of construction |                                | 512        | -                        | 1,513     | (1,671)   | -         | (24)       | 330                     |
|   |                                | 47,669     | 194                      | 2,825     | (280)     | (1,453)   | (1,896)    | 47,059                  |
| Financial assets  |                                |            |                          |           |           |           |            |                         |
| Other loans   |                                | 2,818      | -                        | 1,645     | -         | (1,500)   | (23)       | 2,940                   |
|   |                                | 2,818      | -                        | 1,645     | -         | (1,500)   | (23)       | 2,940                   |
|   |                                | 70,714     | 6,582                    | 5,049     | -         | (3,256)   | (2,060)    | 77,029                  |

The following notes on the consolidated financial statements are part of the consolidated financial statements.

|   | € '000     |           |           |           |                      |            | Cumulated depreciation |            | Residual book values |  |
|---|------------|-----------|-----------|-----------|----------------------|------------|------------------------|------------|----------------------|--|
|   | 01.10.2003 | Additions | Transfers | Disposals | Currency adjustments | 30.09.2004 | 30.09.2004             | 30.09.2003 |                      |  |
| Intangible assets and goodwill                                    |            |           |           |           |                      |            |                        |            |                      |  |
| Goodwill  | 1,934      | -         | -         | -         | (102)                | 1,832      | 16,126                 | 11,116     |                      |  |
| Software  | 200        | 301       | 90        | (16)      | -                    | 575        | 1,315                  | 244        |                      |  |
| Other intangible assets   | 1,898      | 1,348     | 155       | (287)     | -                    | 3,114      | 4,068                  | 4,835      |                      |  |
|   | 4,032      | 1,649     | 245       | (303)     | (102)                | 5,521      | 21,509                 | 16,195     |                      |  |
| Property, plant and equipment                                     |            |           |           |           |                      |            |                        |            |                      |  |
| Land, buildings and leasehold improvement                         | 6,346      | 1,494     | -         | (9)       | (340)                | 7,491      | 18,626                 | 20,877     |                      |  |
| Plant and machinery   | 6,702      | 677       | (4)       | (132)     | (358)                | 6,885      | 1,300                  | 1,567      |                      |  |
| Other fixtures and fittings, tools and equipment                  | 8,621      | 1,585     | (241)     | (1,107)   | (245)                | 8,613      | 3,814                  | 3,044      |                      |  |
| Payments on account and tangible assets in course of construction | -          | -         | -         | -         | -                    | -          | 330                    | 512        |                      |  |
|   | 21,669     | 3,756     | (245)     | (1,248)   | (943)                | 22,989     | 24,070                 | 26,000     |                      |  |
| Financial Assets  |            |           |           |           |                      |            |                        |            |                      |  |
| Other loans   | -          | 69        | -         | -         | -                    | 69         | 2,871                  | 2,818      |                      |  |
|   | -          | 69        | -         | -         | -                    | 69         | 2,871                  | 2,818      |                      |  |
|   | 25,701     | 5,474     | -         | (1,551)   | (1,045)              | 28,579     | 48,450                 | 45,013     |                      |  |

## Notes to the consolidated financial statements for the financial year 2003/2004 (US GAAP)

### (1) The company

#### (a) Business operations

Carl Zeiss Meditec AG, Jena ("Carl Zeiss Meditec" or the "Company") is engaged in the business of developing, manufacturing and marketing medical laser and diagnostic systems. The Company's headquarters are located in Jena, Germany's traditional centre of excellence for optical and optical-related technologies. The Company has subsidiaries in the USA (100%-owned), Japan (51%-owned) and Germany (100%-owned). Together these operations constitute the Carl Zeiss Meditec Group (the "Group").

Carl Zeiss Meditec has so far focused on the ophthalmic market segment. The Company's customers are eye specialists in private practice, optometrists, opticians and clinics worldwide.

#### (b) Basis of presentation

The consolidated financial statements were prepared in compliance with generally accepted accounting principles of the United States of America ("US GAAP").

The financial year of Carl Zeiss Meditec and its subsidiaries ends on 30 September.

### (2) Accounting and valuation principles

#### (a) Principles of consolidation

The consolidated financial statements comprise the annual financial statements of the Company and subsidiaries that the Company controls. The financial position, results of operations and cash flows of enterprises that are controlled by the Company are consolidated. Holdings in enterprises in which the Company exercises a substantial influence, but which it does not control (usually a share of between 20% and 50%) are reflected in the accounts by the equity method. Holdings of less than 20% are reflected in the accounts by the historical cost method if the Company is unable to exercise significant influence and the investee enterprise is not listed on a stock exchange. The effects of intergroup transactions among consolidated companies have been eliminated.

The 49% interest held by outsiders to the Group in the Japanese subsidiary Carl Zeiss Meditec Co. Ltd., Tokyo, Japan, is disclosed as minority interest. A 51% holding in the company was acquired from Carl Zeiss Japan Co., Ltd., Tokyo, Japan on 1 November 2002.

## (b) Conversion of foreign currency

The functional currency of the Company is the euro.

The assets and liabilities of those foreign subsidiaries whose functional currency is other than the euro are translated using the exchange rate as of the reporting date. Capital transactions and balances are converted using the historic rates of exchange in effect at the time the transactions were consummated. The results of operations are converted at the average exchange rate for the financial year. Differences arising from this translation process are shown under "Other comprehensive income / (loss)" within shareholders' equity.

Transactions conducted in foreign currencies are recorded using the rate of exchange in effect at the transaction date. Assets and liabilities denominated in foreign currency, such as cash and cash equivalents, accounts receivable or accounts payable, are remeasured each reporting period until settlement. The resulting income or expenses are shown in the income statement under "Foreign currency gains/(losses)".

The following table shows the exchange rates applied in the preparation of the consolidated financial statements:

|      | Exchange rate on balance sheet date as of |            |        | Average exchange rate |           |        |
|------|---|------------|--------|-----------------------|-----------|--------|
|      | 30.09.2004                                | 30.09.2003 | Change | 2003/2004             | 2002/2003 | Change |
| US\$ | 0.8105                                    | 0.8555     | -5.3%  | 0.8224                | 0.9255    | -11.1% |
| JP¥  | 0.0073                                    | 0.0078     | -6.4%  | 0.0076                | 0.0078    | -2.6%  |

## (c) Use of estimates

The preparation of annual financial statements in accordance with US GAAP requires the use of certain assumptions and estimates. These assumptions relate to the recognition and measurement of assets and liabilities, the nature and extent of contingent liabilities at the balance sheet date and the amount of income and expenses in the reporting period. Actual results may differ from these estimates.

**(d) Cash and cash equivalents**

Cash and cash equivalents held in banks as well as liquid securities with an original maturity of less than three months are reported as cash and cash equivalents. Because of their short maturity, the carrying amounts of cash and cash equivalents are approximately equal to their fair value.

Restricted cash of € 850,000 as of 30 September 2003 represented collateral for the purchase of business assets.

**(e) Accounts receivable and loans**

Trade accounts receivable and loans are disclosed at their nominal value, net of possible allowance for estimated uncollectible accounts.

Valuation allowances are established for doubtful receivables and loans associated with discernible risks. Unrecoverable receivables and loans are written off. Long-term interest free receivables and loans are discounted based on market conditions; accrued interest is shown as income by the effective interest method.

**(f) Inventories**

Inventories are valued at the lower of acquisition/manufacturing cost or market value. Costs are primarily determined on the basis of the weighted average cost method. Manufacturing costs include materials and labour, as well as direct manufacturing and material overheads including depreciation.

**(g) Property, plant and equipment**

Property, plant and equipment are reported at cost, net of accumulated depreciation. Depreciation is calculated using the straight-line method over the estimated useful economic life of each asset. The following depreciation periods are applied:

|   |            |
|---|------------|
| Buildings and leasehold improvements                                  | 3-44 years |
| Plant and machinery, other fixtures and fittings, tools and equipment | 1-23 years |

Leasehold improvements are depreciated over their customary service life. This is limited, however, to the term of the rental or lease agreement. Customary service life is evaluated regularly by the Company's management in the light of current technological conditions. Maintenance and repairs are charged to expenses as incurred, while renewals and improvements that extend the useful life or increase capacity are capitalised. Upon the sale or retirement of property and equipment, the accounts are relieved of the cost and related accumulated depreciation, with any resulting gain or loss disclosed in the income statement under "General and administrative expenses".

### **(h) Goodwill**

Starting 1 October 2002, Carl Zeiss Meditec AG adopted Statement of Financial Accounting (SFAS) No. 142, "Goodwill and Intangible Assets". Under SFAS No. 142 goodwill is no longer amortised. Scheduled amortisation of goodwill is no longer reflected in the consolidated income statement beginning with the financial year 2002/2003.

Prior to the application of SFAS No. 142, goodwill was amortised over its anticipated useful life. Such goodwill only represented the excess of purchase cost over the acquired net assets of Humphrey Instruments, Inc. ("Humphrey"), a subsidiary of Allergan Inc., in 1991. This goodwill was originally amortised by the straight-line method over its anticipated useful life of 15 years.

In 2002 the former Carl Zeiss Ophthalmic Systems AG purchased Asclepion Meditec AG in a transaction accounted for as a reverse acquisition. The acquisition resulted in goodwill valued at € 15.216 million.

With respect to the transfer of the ophthalmic distribution activities of Asclepion-Meditec S.R.L., Milan, Italy to Carl Zeiss S.p.A., Arese, Italy with effect from 1 February 2003, at book value within the scope of an asset deal, goodwill as shown in the consolidated balance-sheet decreases by € 1.099 million, which is the amount allocated to Asclepion-Meditec S.R.L. (see Note 3). Moreover, in the financial year 2002/2003 the deferred tax liabilities assumed for the purchase price allocation carried out in the previous year, which appeared to be too conservative, were adjusted by € 3.744 million. The adjustment was set off against goodwill with no effect on income.

Goodwill of € 5.049 million resulted from the acquisition of hiko medical communication GmbH in Pirmasens (now Carl Zeiss Meditec Systems GmbH) on 17 December 2003 (see Note 3).

The book value of goodwill was allocated to the following segments (For explanation of segments see Note 23):

| € '000   | Financial year 2003/2004 |                      |           | Financial year 2002/2003 |                      |           |           |
|----------|--------------------------|----------------------|-----------|--------------------------|----------------------|-----------|-----------|
|          | 30.09.2004               | Currency adjustments | Additions | 30.09.2003               | Currency adjustments | Additions | Disposals |
| Segment  |                          |                      |           |                          |                      |           |           |
| Germany  | 15,422                   | -                    | 5,049     | 10,373                   | -                    | -         | 4,843     |
| USA      | 704                      | (39)                 | -         | 743                      | (139)                | -         | -         |
| Goodwill | 16,126                   | (39)                 | 5,049     | 11,116                   | (139)                | -         | 4,843     |

Upon adoption of SFAS No. 142, Carl Zeiss Meditec assessed whether previously recognised intangible assets and goodwill conform to the criteria of the new standard on the day of first application. The Company examined the classification, estimated useful lives and residual book values of all intangible assets and determined that no adjustments were necessary, both in relation to the carrying amount of such assets as well as their estimated remaining useful lives.

Carl Zeiss Meditec also examined whether goodwill would be impaired as of 1 October 2002 under the new provisions of SFAS No. 142. For this purpose, Carl Zeiss Meditec determined (1) the Company's reporting units, (2) the respective net assets of each reporting unit after the assignment of Company's assets and liabilities including existing goodwill and intangible assets to these reporting units and (3) the fair value of the reporting units. The Company concluded that there was no indication of a loss in value of goodwill in any of the Group's reporting units as of 1 October 2002.

Carl Zeiss Meditec completed the annual impairment test of goodwill in the last quarter of the financial year 2003/2004. The results of this test did not indicate any impairment of goodwill as at 30 September 2004.

With regard to the change in goodwill in the financial year 2003/2004 please refer to the consolidated fixed-asset movement schedule and Note 3.

### **(i) Other intangible assets**

Other intangible assets are valued at acquisition cost minus accumulated depreciation and written off over an average term of 5 years (see Note 3).

### **Software development costs**

The Company accounts for its software development costs in accordance with SFAS No. 86, "*Accounting for Costs of Computer Software to be Sold, Leased or Otherwise Marketed*". Capitalisation of software development costs begins upon establishment of technological feasibility and ends upon general release of the software for sale. Costs incurred after technological feasibility is established are not material and, accordingly, are expensed when incurred.

### **(j) Non-current assets**

The Company reviews its non-current assets, including intangible assets and property, plant and equipment, whenever events or changed circumstances indicate that the book value of an asset may be impaired. To determine whether an asset is impaired, its carrying value is compared with the future non-discounted cash flow expected to be generated by the asset. If the carrying value of the asset or assets exceeds the future expected non-discounted cash flows, the asset is deemed to be impaired. Fair value is generally based on either an appraised value or measured by alternative techniques, such as discounted cash flow analysis.

### **(k) Leasing**

The Company has leased certain assets under long-term contracts. All property under arrangements that qualify as capital lease are carried as long-term assets pursuant to SFAS No. 13 "*Accounting for Leases*". The corresponding leasing obligations are carried as long-term liabilities according to their time to maturity. Other leasing transactions are treated as so-called operating lease; the respective lease payments are recorded on a straight-line basis as expenses.

## (l) Financial instruments and risk provisioning

Fair value of financial instruments – The fair value of a financial instrument is the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced sale or liquidation. The financial instruments of the Company primarily consist of cash and cash equivalents, accounts receivable from group cash management of Carl Zeiss Financial Services GmbH, Oberkochen (Treasury), trade accounts receivable, trade accounts payable, short-term debt and other current liabilities. Because of the short-term nature of these financial instruments, the fair value of all financial instruments approximate their carrying values as of 30 September 2004 and 2003. (Refer to Note 16 for further information)

Derivative financial instruments – As a company with global operations, Carl Zeiss Meditec is exposed to the risk of currency rate fluctuations and has entered into currency forward contracts and options to hedge against its exchange risks on the basis of planned transactions in foreign currencies. These contracts generally cover a period of less than one year.

The nominal value of these contracts is not reflected in the consolidated financial statements. Instead, the contracts are measured at their fair value as at 30 September 2004 and 2003 and are disclosed as current assets or liabilities in the consolidated financial statements. Changes in the fair value of these derivative instruments are recognised each reporting period in the consolidated income statement as a currency gain or loss. The management is regularly involved in such decisions on risk provisioning. The Company does not own any derivative financial instruments for trading purposes, nor does it issue such contracts.

Profit or loss from the revaluation of derivative financial instruments not yet due in the amount of € -493,000 (previous year € -304,000) are recorded under "Foreign currency gains / (losses)" in the income statement.

The market values of derivatives and other financial instruments are outlined in Note 16.

## (m) Pension obligations

### Defined contribution pension plans

The US subsidiary offers a savings scheme to the majority of its employees. This savings scheme is a so-called defined contribution plan pursuant to *Section 401 (k) of the Internal Revenue Code*. The plan enables the participating employees to save a proportion of their income in accordance with the specified guidelines. The Company is currently matching a percentage of employee contributions up to a certain limit. The "matching contributions" of the Company for the "401(k) plan" amounted to € 1.221 million in the financial year 2003/2004 and to € 1.267 million in the financial year 2002/2003.

**Defined benefit pension plans**

The Company offers defined benefit pension plans to certain employees. Such benefits are determined primarily by the employee's remuneration and length of service. Pension obligations and related costs are calculated by the prescribed projected unit credit method in accordance with SFAS No. 87 "*Employers' Accounting for Pensions*". The projected unit credit method reflects economic assumptions based on long-term expectations, as well as the performance of assets legally set aside to fund future benefit payments.

With effect from 1 January 2000 a company pension scheme based on the so-called "Benefit Regulations 2000" was established. Future benefits are calculated from the total pension units purchased during the period of employment starting 1 January 2000, calculated as the product of an annual total contribution and an age-related pension factor. The annual total contribution for individual employees is calculated as the sum of a basic contribution (1%) and a profit-related contribution based on the company's success (between 0% and 3%), calculated as a percentage of the individual benefit-related income. The Company has committed itself to raising ongoing benefit payments by 1% each year. This guaranteed adjustment is taken into account in the valuation.

In addition, accruals of € 111,000 and € 72,000 for 30 September 2004 and 30 September 2003 respectively reflect deferred compensation of Company employees.

Actuarial profits or losses that may arise from changes in the valuation premises or from a deviation in actual versus expected performance are only reflected in income if the balance of the accumulated actuarial profits or losses amounts to more than 10% of the projected benefit obligation or the market related value of plan assets under the defined pension plans. Any amount that lies outside the 10% corridor is recorded to income over the average residual term of service of employees eligible for pensions, which at 30 September 2004 is estimated to be 15 years.

**(n) Taxes on income and earnings**

Taxes on income and earnings are computed annually by the asset and liability method pursuant to SFAS No. 109 "Accounting for Income Taxes". All liabilities or claims relating to taxes on income, earnings, capital and property arising during the financial year are reflected in the consolidated financial statements pursuant to the relevant tax laws. Deferred tax assets and liabilities are calculated each year for differences between the consolidated financial statement carrying amounts and tax bases of assets and liabilities, based on enacted tax laws and rates applicable to the periods in which the differences are expected to affect taxable income. Valuation allowances are established for deferred tax assets as necessary to reflect the net amount that is more likely than not to be realised. Income tax expense comprises the tax payable or refundable for the reporting period, plus or minus the change in deferred tax. The effects of a change in tax rates on deferred tax assets and liabilities are recognised in income for the period in which the change was enacted.

**(o) Recording of revenues**

The Company generates sales from selling products and services on the basis of contracts. A sale is effected when all the parts of the product have been delivered or the service has been provided, the risks have passed, the payment is agreed or can be determined, no substantial obligations towards the customers are outstanding, and collectibility of the receivable is deemed reasonably assured. Sales are reflected net of dealer commissions, trade discounts, customer allowances and rebates.

Dealer commissions amounted to € 3.598 million and € 3.061 million respectively in the financial years 2003/2004 and 2002/2003.

Maintenance revenue from service contracts is realised as services are rendered throughout the contractual period of performance.

**(p) Advertising**

Advertising costs are treated as expenses. In the 2003/2004 and 2002/2003 financial years advertising costs amounted to € 2.680 million and € 2.630 million, respectively and were recorded as a component of selling and marketing expense.

### **(q) Product-related costs**

Research and development costs and marketing and selling expenses are charged to expenses as incurred. Research and development subsidies are set off against the related expenses at the time the entitlement arises.

The Company furnishes the buyer with a warranty for the perfect functioning of sold products for the contractually agreed period of 15 months. For this purpose, provisions are formed on the basis of the average values of warranty claims made in the past. These provisions are regularly adjusted to reflect actual experience. Such provisions are recorded as cost of goods sold in the same period that the initial sale is recorded.

The Company discloses freight costs charged to customers as a component of sales and reflects the corresponding freight costs in the cost of goods sold. In the financial year 2003/2004 the shipping and handling costs not billed to customers amount to € 3.344 million (previous year: € 2.604 million) and are shown in the selling and marketing expenses.

### **(r) Other comprehensive income/loss**

SFAS No. 130 *“Reporting Comprehensive Income”* requires the disclosure of “Other comprehensive income”. Other comprehensive income comprises net income/loss for the period as well as all other equity changes or “Other comprehensive income/loss” that have no effect on the operating result but that are not related to transactions with shareholders. Refer to Note 20 for further information.

### **(s) Earnings/loss per share**

Basic earnings/loss per share was calculated by dividing the net income/loss for the year by the weighted average number of common shares issued in the relevant accounting period. Earnings/loss per share allowing for the effects of dilution was calculated in compliance with SFAS No. 128, *“Earnings per Share”*, such that the effect of potentially dilutive securities is reflected.

The following table shows the calculation of basic and diluted earnings per share:

|   | Financial year 2003/2004 | Financial year 2002/2003 |
|---|--------------------------|--------------------------|
| Consolidated net income (in € '000)                                 | 12,610                   | 6,558                    |
| Weighted average of issued shares, basic                            | 28,402,339               | 25,918,166               |
| Dilution effect of stock options                                    | -                        | -                        |
| Weighted average of issued shares, allowing for the dilution effect | 28,402,339               | 25,918,166               |
| Earnings per share (in €)   | 0.44                     | 0.25                     |

The dilution effect would be calculated using the *treasury stock method*. However, because the average market values of the Company's common stock during the period were less than the exercise price of all stock options outstanding, stock options result in no dilutive effect on earnings/loss per share at 30 September 2004 and 2003. As of 30 September 2004 the Company had issued 105,500 stock options that would result in a dilution effect.

#### (t) Stock option plan

The Company posts its stock option plan in accordance with the *"intrinsic value method"* prescribed by Accounting Principles Board (APB) Opinion No. 25, *"Accounting for Stock Issued to Employees"* and respective interpretations. Pursuant to APB No. 25, remuneration expenses for stock options are calculated on the basis of the intrinsic value at the measurement date. Intrinsic value is calculated from the difference between the market value of the shares on the *measurement date* and the exercise price. The measurement date is the point in time at which the number of shares to which the beneficiary is entitled and the purchase price are known. SFAS No. 123 *"Accounting for Stock-Based Compensation"* mandates disclosure of the compensation expenses for stock-based remuneration that would have been recorded under the *"fair value method"*. Under this method, compensation expense is calculated based on the fair value of the award at the time the stock options are granted. This compensation expense is recognised over the period through to the earliest point in time at which they may be exercised. SFAS 148 *"Accounting for Stock-Based Compensation, Transition and Disclosure"* also requires the disclosure of the pro forma effect of using the fair value method of accounting for stock-based employee compensation.

The Company has elected to apply the provisions of APB No. 25 and to follow the disclosure stipulations of SFAS No. 123 and No. 148 (see Note 18).

Had the fair value method defined in SFAS No. 123 been employed in the calculation of the remuneration expenses, net income for the year and the earnings per share would have been as follows:

| € '000   | Financial year 2003/2004 | Financial year 2002/2003 |
|--|--------------------------|--------------------------|
| Consolidated net income, as posted                       | 12,610                   | 6,558                    |
| Stock options expenses (after tax) according to SFAS 123 | (33)                     | (110)                    |
| Pro forma consolidated net income                        | 12,577                   | 6,448                    |
| Earnings per share (€):                                  |                          |                          |
| as posted  | 0.44                     | 0.25                     |
| pro forma  | 0.44                     | 0.25                     |
| Earnings per share allowing for the dilution effect (€): |                          |                          |
| as posted  | 0.44                     | 0.25                     |
| pro forma  | 0.44                     | 0.25                     |

### (u) Public subsidies

Subsidies for investments such as investment grants and tax-free investment premiums are disclosed as income (as a reduction in depreciation) over the useful life of the subsidised fixed assets. Unrecognised investment premiums are reported as deferred income on the balance sheet, whereas investment grants are subtracted from the acquisition or production costs of the related fixed assets.

Other subsidies which are taxable are disclosed under research and development expenses.

Public subsidies received in the financial years 2003/2004 and 2002/2003 are listed in Note 15.

**(v) Recent pronouncements on accounting principles**

In January 2003, the FASB issued FASB Interpretation No. 46, "*Consolidation of Variable Interest Entities – and Interpretation of ARB No. 51*", ("FIN 46"). FIN 46 was subsequently amended in December 2003.

FIN 46 changes the current practice of solely determining whether consolidation is appropriate based only on control, which is generally demonstrated through the ownership of a majority of voting interests in an entity. Under the new Interpretation a reporting company has to assess if the entities with which it has business relationships are *Variable Interest Entities* ("VIE") or *Voting Interest Entities*. VIEs are entities in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at the risk for the entity to finance its activities without additional subordinated financial support from other parties.

If an entity is a VIE, the reporting company is required to assess if it has a variable interest ("VI") in the VIE. VIs in a VIE are contractual, ownership, or other pecuniary interests in an entity that change with changes in the entity's net asset value. Equity interests with or without voting rights are considered variable interests if the entity is a VIE.

FIN 46 explains how to identify VIEs and how an enterprise should assess its interest in a VIE.

If the reporting company has a VI in the VIE, it must assess whether it, or another VI holder, is the primary beneficiary of the VIE. FIN 46 requires existing unconsolidated VIEs to be consolidated by their primary beneficiaries. The primary beneficiary of a variable interest entity is the party that absorbs a majority of the VIE's expected losses, receives a majority of its expected residual returns, or both.

This Interpretation applies immediately to VIEs created after 31 January 2003, and to VIEs in which an enterprise obtains an interest after that date. Otherwise FIN 46 is applicable on the last day of the first interim or annual period ending after 15 December 2003 - that is, 31 December 2003 for Carl Zeiss Meditec. The amendments to FIN 46 became effective during the quarter ended 31 March 2004. The application of FIN 46 had no impact on the Company's financial statements.

In December 2003 the FASB issued Statement SFAS No. 132 (revised 2003) *“Employers’ Disclosures about Pensions and Other Postretirement Benefits”*. This statement requires that companies provide a detailed annual account of their trust funds, projected unit credits, cash flows, net expenses from pension and health care commitments for retirees and other relevant items. In addition, companies must submit a quarterly report on the individual net expense items for pension and health care commitments for retirees. SFAS No. 132 (revised) was applicable as of 31 December 2003. Accordingly, the standard was taken into account for the first time in the 1st quarter of 2003/2004 and the detailed notes published as required.

### **(3) Business acquisitions and sales**

#### **Transactions in the financial year 2003/2004**

##### **Carl Zeiss Meditec Systems GmbH, Pirmasens**

On 17 December 2003 Carl Zeiss Meditec AG acquired a 100% interest in the former hiko medical communication GmbH of Pirmasens. The company now operates under the name Carl Zeiss Meditec Systems GmbH. Carl Zeiss Meditec Systems GmbH specialises in the development of medical software solutions and under the name VISUPAC™ it markets a successful product (including related services) that enables filing and management of diagnostic and treatment data by eye specialists and clinics. Furthermore, Carl Zeiss Meditec Systems GmbH has an efficient team of development, marketing and service specialists at its disposal. With the acquisition of this company, Carl Zeiss Meditec has taken a further major step in the implementation of its strategy. Carl Zeiss Meditec will secure the necessary resources and know how to enable it to offer customers cross-platform software solutions for ophthalmic applications.

Activities of the acquired company are reflected in the consolidated financial statements from 17 December 2003, the day of acquisition.

The acquisition price amounted to € 6.094 million, which was funded entirely in cash. Direct acquisition costs amounted to € 66,000.

The following table shows a breakdown of the purchase price (including direct acquisition costs) at the time of acquisition (*Purchase Price Allocation / PPA*) in conformance with SFAS No. 141.

| € '000   |              |
|--|--------------|
| Current assets purchased                                     | 2,883        |
| Property, plant and equipment purchased                      | 194          |
| Other intangible assets purchased                            | 21           |
| Purchase Price Allocation:                                   |              |
| Computer software  | 1,318        |
| Goodwill   | 5,049        |
| <b>Purchased assets and Purchase Price Allocation, total</b> | <b>9,465</b> |
| Assumed current liabilities                                  | (2,675)      |
| Assumed other non-current liabilities                        | (630)        |
| <b>Total acquisition costs</b>                               | <b>6,160</b> |

Intangible assets (computer software) identified within the scope of purchase price allocation are written off over an average term of five calendar years.

The acquisition resulted in a non-tax deductible goodwill valued at € 5.049 million. In accordance with SFAS No. 141, amortisation was not recorded on this amount. Instead, the acquired goodwill is subject to *impairment testing* provisions of SFAS No. 142.

On a pro forma basis, the effects of the acquisition on previously reported results would be immaterial, assuming that the business combination hypothetically been consummated as of 1 October 2003. It should be noted that Carl Zeiss Meditec Systems GmbH (formerly hiko medical communication GmbH) generates the majority of its revenue through business with Carl Zeiss Meditec. This means the consolidation will have virtually no impact on the consolidated sales.

For the reasons given above, no pro forma values were given.

### Transactions in the financial year 2002/2003

#### Carl Zeiss Meditec Co., Ltd., Tokyo, Japan

On 1 November 2002 Carl Zeiss Meditec acquired at book value a 51% holding in the Japanese Carl Zeiss Meditec Co., Ltd., from Carl Zeiss Co., Ltd. This acquisition was accounted for as a transaction under common control, as the controlling shareholder of Carl Zeiss Meditec was also the majority shareholder in Japanese Carl Zeiss Meditec Co., Ltd. Accordingly, the assets and liabilities acquired were carried over at book values.

The following is a summary of the assets acquired and liabilities assumed in the course of the acquisition.

| € '000                                   |       |
|--|-------|
| Book value of the acquired assets        | 2,170 |
| Assumed liabilities                      | 1,637 |
|  | 533   |
| Payment for acquisition of holding (51%) | (272) |
| Minority interest                        | (261) |
|  | 0     |

The balance sheet includes a caption entitled "Minority interests". This caption represents the equity holdings in the subsidiary Carl Zeiss Meditec Co., Ltd. that are attributable to third parties (Carl Zeiss Japan Co., Ltd.).

As the transaction was accounted for at historical cost, no goodwill arose.

#### **Asclepion-Meditec S.R.L., Milan, Italy**

On 1 February 2003 the ophthalmic distribution activities (Vision) of Asclepion-Meditec S.R.L., Milan, Italy, a subsidiary of Carl Zeiss Meditec, was transferred to an affiliate, Carl Zeiss S.p.A. Arese, Italy, at book value as an asset deal. As a distributor for the Italian market, Carl Zeiss S.p.A., Arese, Italy, will continue to process and fulfil the orders for the Company's Vision product line. The transaction resulted in a € 200,000 increase in the net working capital position of Carl Zeiss Meditec.

In conjunction with the transfer, the goodwill shown in the consolidated balance sheet was reduced by the amount of € 1.099 million attributable to Asclepion-Meditec S.R.L.

#### **Carl Zeiss Meditec Ltd. (previously Asclepion-Meditec Ltd.), Edinburgh, Scotland**

The Group company Carl Zeiss Meditec Ltd., Edinburgh, Scotland, has likewise been restructured. With effect from 1 February 2003, the Vision Business Unit was transferred to the affiliated company Carl Zeiss Ltd. at Welwyn Garden City, UK. As a distributor for the UK market, Carl Zeiss Ltd. will continue to process and fulfil orders for the Vision division throughout UK. In addition, the Dental Business Unit of Carl Zeiss Meditec Ltd. was sold to Denfotex Ltd., Wynham, UK. This transaction resulted in a minor net loss on sale of € 16,000 as disclosed in the income statement under "General and administrative costs".

**Asclepion-Meditec Inc., Coto de Caza, USA**

The wholly-owned subsidiaries Asclepion-Meditec USA, and Carl Zeiss Meditec, Inc., Dublin, USA, were merged with effect from 1 January 2003. The merger process had no impact on the consolidated financial statements.

**Discontinued Aesthetic and Dental operations**

In the previous year as of 1 May 2003 Carl Zeiss Meditec sold the dermatological and dental laser divisions that were not part of its core business to the Italian companies EL.EN S.P.A., Florence, and Quanta System S.P.A., Milan.

In accordance with the accounting rules set forth in SFAS No. 144 *“Accounting for the Impairment or Disposal of Long-Lived Assets”* this disposal was identified as *“Discontinued operations”*. The consolidated income statement was adjusted to take account of these operations. The revenue from the sale of business units is shown in the income statement under *“Net income from discontinued operations”*. The balance sheet and corresponding notes in the previous year were retroactively restated for the purposes of comparison and in accordance with SFAS No. 144. The share of sales and pre-tax profits of discontinued dermatological and dental operations were as follows:

| € '000                        | Financial year 2003/2004 | Financial year 2002/2003 |
|-------------------------------|--------------------------|--------------------------|
| Revenues                      | -                        | 4,705                    |
| Result before taxes on income | -                        | (5,934)                  |

The discontinued operations were mainly part of the geographic segment *“Germany”*.

As of 30 September 2003 the balance sheet already contained no assets or debts from discontinued activities.

The total proceeds from the disposal of the discontinued operations were € 2.5 million. Of this figure, € 1.0 million was immediately recorded as revenue. The remaining € 1.5 million had been secured by a bank guarantee in favour of Carl Zeiss Meditec and was paid in January 2004.

## (4) Business relationships to affiliated companies

The Company separately reports liabilities to and receivable from affiliated companies. The designation "affiliated companies" comprises Carl Zeiss AG and its subsidiaries.

For the purposes of furnishing the Company with short-term funds and investing surplus liquidity, Carl Zeiss Meditec has been integrated into the group cash management system of Carl Zeiss Financial Services GmbH, Oberkochen (Treasury). Loans paid or funds invested within the scope of this business relationship are shown as liabilities due to or receivables due from affiliated companies (Treasury). Loans and receivables carry interest at a rate based on the 1-month EURIBOR and conform to normal market conditions.

In addition to cash management the Company utilises various services from the Carl Zeiss Group, in particular from Carl Zeiss Jena GmbH. Contractual arrangements exist by which Carl Zeiss Jena GmbH provides, for example, research and development services, personnel and administrative functions as well as logistics, marketing and computing activities.

The Company has a number of agreements with the companies of the Carl Zeiss AG resulting in the following accounts payable and receivable, sales and expenses:

| € '000                          | 30.09.2004    | 30.09.2003    |
|---------------------------------|---------------|---------------|
| Accounts receivable             |               |               |
| Treasury                        | 27,352        | 12,089        |
| Carl Zeiss AG                   | 1,396         | 531           |
| Carl Zeiss Co., Ltd., Japan     | 912           | 403           |
| Carl Zeiss Ltd., United Kingdom | 607           | -             |
| Carl Zeiss S.p.A., Italy        | 1,435         | 2,779         |
| Carl Zeiss S.A.S., France       | 603           | 878           |
| Carl Zeiss S.A., Spain          | 796           | 700           |
| Other                           | 2,814         | 3,071         |
| <b>Total</b>                    | <b>35,915</b> | <b>20,451</b> |

| € '000                                   | 30.09.2004   | 30.09.2003   |
|--|--------------|--------------|
| Accounts payable                         |              |              |
| Treasury                                 | -            | 37           |
| Carl Zeiss AG                            | 365          | 53           |
| Carl Zeiss Jena GmbH                     | 1,394        | 1,825        |
| Carl Zeiss de Mexico S.A.de C.V., Mexico | 409          | 384          |
| Carl Zeiss Co., Ltd., Japan              | 2,209        | 2,489        |
| Carl Zeiss Holding Co., Inc., USA        | 31           | 33           |
| Other                                    | 664          | 1,098        |
| <b>Total</b>                             | <b>5,072</b> | <b>5,919</b> |

| € '000                                   | Financial year 2003/2004 | Financial year 2002/003 |
|--|--------------------------|-------------------------|
| Sales                                    |                          |                         |
| Carl Zeiss AG                            | 2,283                    | 1,311                   |
| Carl Zeiss Ltd., United Kingdom          | 5,340                    | 5,049                   |
| Carl Zeiss S.p.A., Italy                 | 6,550                    | 7,112                   |
| Carl Zeiss S.A., Spain                   | 4,506                    | 5,954                   |
| Carl Zeiss Co., Ltd., Japan              | -                        | 1,021                   |
| Carl Zeiss Far East Co. Ltd., Kowloon    | 6,963                    | 3,863                   |
| Carl Zeiss S.A.S., France                | 4,561                    | 4,690                   |
| Carl Zeiss Co. Ltd., South Korea         | 2,795                    | 2,155                   |
| Carl Zeiss de Mexico S.A.de C.V., Mexico | 2,832                    | 2,155                   |
| Carl Zeiss Canada Ltd., Canada           | 3,852                    | 3,200                   |
| Carl Zeiss GmbH, Austria                 | 2,703                    | 2,315                   |
| Carl Zeiss Pty. Ltd., Australia          | 2,449                    | 1,694                   |
| Carl Ziess N.V.-S.A., Belgium            | 1,488                    | -                       |
| Other                                    | 10,136                   | 8,760                   |
| <b>Total</b>                             | <b>56,458</b>            | <b>49,279</b>           |

The Company purchased the following goods (inventories):

| € '000                      | Financial year 2003/2004 | Financial year 2002/003 |
|-----------------------------|--------------------------|-------------------------|
| Cost of goods delivered     |                          |                         |
| Carl Zeiss AG               | 729                      | 1,157                   |
| Carl Zeiss Jena GmbH        | 10,965                   | 10,646                  |
| Carl Zeiss Co., Ltd., Japan | 4,511                    | -                       |
| Other                       | 416                      | 643                     |
| <b>Total</b>                | <b>16,621</b>            | <b>12,446</b>           |

The Company also purchased the following services:

| € '000                             | Financial year 2003/2004 | Financial year 2002/003 |
|------------------------------------|--------------------------|-------------------------|
| Services                           |                          |                         |
| Carl Zeiss AG                      | 2,638                    | 1,557                   |
| Carl Zeiss Jena GmbH               | 6,690                    | 7,699                   |
| Carl Zeiss Co., Ltd., Japan        | 6,312                    | 13,955                  |
| Carl Zeiss Financial Services GmbH | 607                      | -                       |
| Carl Zeiss Holding Co., Inc., USA  | 230                      | 352                     |
| Other                              | 202                      | 976                     |
| <b>Total</b>                       | <b>16,679</b>            | <b>24,539</b>           |

Purchased services include € 1.990 million in research and development costs commissioned with Carl Zeiss Group for the financial year 2003/2004 (previous year: € 2.276 million).

## (5) Trade accounts receivable

| € '000                           | 30.09.2004    | 30.09.2003    |
|----------------------------------|---------------|---------------|
| Current accounts receivable      | 38,275        | 40,822        |
| Long-term accounts receivable    | 405           | 765           |
| Provisions for bad debts         | 12,044        | 10,525        |
| <b>Trade accounts receivable</b> | <b>26,636</b> | <b>31,062</b> |

Long-term accounts receivable are recorded on a discounted basis and accredited to face value over the term of each receivable. The discount was € 12,000 as of 30 September 2004 and € 12,000 as of 30 September 2003.

## (6) Other current assets

Other current assets are comprised as follows:

| € '000   | 30.09.2004   | 30.09.2003   |
|--|--------------|--------------|
| Accounts receivable from R&D subsidies                       | 538          | 495          |
| Derivative financial instruments                             | 141          | 436          |
| Accounts receivable from tax authorities                     | 40           | -            |
| Accounts receivable from the sale of discontinued operations | -            | 1,811        |
| Other accounts receivable                                    | 489          | 1,730        |
| <b>Other current assets</b>                                  | <b>1,208</b> | <b>4,472</b> |

## (7) Inventories

The inventories (net) comprise:

| € '000                          | 30.09.2004    | 30.09.2003    |
|---------------------------------|---------------|---------------|
| Raw materials and supplies      | 15,435        | 17,106        |
| Work in progress                | 7,623         | 7,325         |
| Finished goods                  | 19,178        | 21,337        |
| Advances made                   | 77            | 34            |
| <b>Total inventories, gross</b> | <b>42,313</b> | <b>45,802</b> |
| Provisions for bad debts        | 8,187         | 7,191         |
| <b>Total inventories, net</b>   | <b>34,126</b> | <b>38,611</b> |

## (8) Property, plant and equipment

Property, plant, and equipment comprise:

| € '000  | 30.09.2004    | 30.09.2003    |
|---|---------------|---------------|
| Land, buildings and leasehold improvements                  | 26,117        | 27,223        |
| Plant and machinery   | 8,185         | 8,269         |
| Other fixtures and fittings, tools and equipment            | 12,427        | 11,665        |
| Advances made and tangible assets in course of construction | 330           | 512           |
|   | 47,059        | 47,669        |
| Minus: accumulated depreciation                             | 22,989        | 21,669        |
| <b>Property, plant and equipment, net</b>                   | <b>24,070</b> | <b>26,000</b> |

Depreciation amounted to € 3.756 million and € 4.317 million respectively for the financial years 2003/2004 and 2002/2003.

The posted property, plant, and equipment include leased assets with a net book value of approximately € 13.265 million. These assets have a gross balance of € 20.899 million, accumulated depreciation at 30 September 2003 is € 7.634 million. Depreciation on leased assets is included in the depreciation expense.

## (9) Other intangible assets

The item "Other intangible assets" comprises exclusively the following assets subject to amortisation:

| € '000                       | 30.09.2004                       |                            |               | 30.09.2003                       |                            |               |
|------------------------------|----------------------------------|----------------------------|---------------|----------------------------------|----------------------------|---------------|
|                              | Costs of purchase/<br>conversion | Cumulative<br>depreciation | Book<br>value | Costs of purchase/<br>conversion | Cumulative<br>depreciation | Book<br>value |
| Customer base                | 2,270                            | 1,021                      | 1,249         | 2,270                            | 567                        | 1,703         |
| Patents                      | 2,105                            | 947                        | 1,158         | 2,105                            | 526                        | 1,579         |
| Technology                   | 1,586                            | 714                        | 872           | 1,586                            | 397                        | 1,189         |
| Trademarks / Tradenames      | 485                              | 218                        | 267           | 485                              | 121                        | 364           |
| Licenses                     | 685                              | 203                        | 482           | -                                | -                          | -             |
| Software                     | 1,890                            | 575                        | 1,315         | 444                              | 200                        | 244           |
| Other                        | 51                               | 11                         | 40            | -                                | -                          | -             |
| <b>Intangible assets</b>     | <b>9,072</b>                     | <b>3,689</b>               | <b>5,383</b>  | <b>6,890</b>                     | <b>1,811</b>               | <b>5,079</b>  |
| Less discontinued operations | -                                | -                          | -             | 98                               | 98                         | -             |
| <b>Intangible assets</b>     | <b>9,072</b>                     | <b>3,689</b>               | <b>5,383</b>  | <b>6,792</b>                     | <b>1,713</b>               | <b>5,079</b>  |

Depreciation and amortisation amounted to € 1.649 million and € 1.458 million respectively for the financial years 2003/2004 and 2002/2003.

Estimated depreciation on other intangible assets for the next five years is as follows:

| Year (€ '000) |       |
|---------------|-------|
| 2004/2005     | 1,719 |
| 2005/2006     | 1,718 |
| 2006/2007     | 1,315 |
| 2007/2008     | 324   |
| 2008/2009     | 124   |

Besides the goodwill shown in the consolidated financial statements, Carl Zeiss Meditec has no intangible assets that are not subject to scheduled depreciation.

## (10) Financial assets

The following table shows the change in financial assets from 1 October 2003 to 30 September 2004:

| € '000             | Financial year 2003/2004 |
|--------------------|--------------------------|
| Value as of 01.10. | 2,818                    |
| Addition           | 1,645                    |
| Disposal           | (1,500)                  |
| Other              | (92)                     |
| Value as of 30.09. | 2,871                    |

The balance sheet item "Loans" was increased by the granting of a loan of € 1.625 million (US\$ 2.0 million) to alliance partner Notal Vision, Inc. Carl Zeiss Meditec is cooperating with Notal Vision in the field of early diagnosis of age-related macular degeneration (AMD). The loan bears 4% interest p.a. and is due to be repaid by December 2006.

In the event of failure to repay the amount owed, Carl Zeiss Meditec has retained the right to demand 30% of the sales proceeds accrued by Notal Vision, Inc. on the basis of a purchase contract between the two companies. In addition, at the Company's discretion the outstanding loan amount may be converted at any time into preferred shares in Notal Vision, Inc. or the term for repayment extended.

In connection with a suit for damages against I-Spire s.p.r.l., Brussels/Belgium and its sole proprietor, an out-of-court settlement was reached in the second quarter of the financial year 2003/2004. This settlement provides for the payment of the total amount shown in the balance sheet item "Loans" by I-Spire s.p.r.l. in accordance with a payment plan. The first instalment of € 1.5 million was paid at the end of April 2004.

## (11) Provisions

The provisions comprise the following:

| € '000   | 30.09.2004    | 30.09.2003    |
|--|---------------|---------------|
| Provisions for personnel expenses                | 9,945         | 9,446         |
| Provisions for outstanding invoices and services | 6,655         | 4,985         |
| Warranty provisions                              | 4,642         | 3,856         |
| Provisions for taxation                          | 713           | 807           |
| Provisions for licenses                          | 363           | 666           |
| Provisions for commissions                       | 327           | 291           |
| Other  | 786           | 476           |
| <b>Total provisions</b>                          | <b>23,431</b> | <b>20,527</b> |

As of 30 September 2004 and 2003 provisions for personnel expenses comprised provisions for pension as well as provisions in connection with the "401 (k) Plan" to the amount of € 1.511 million and € 0.839 million respectively.

### Provisions for warranty payments

The following table shows the change in warranty provisions from 1 October 2003 to 30 September 2004:

| € '000                    | Financial year 2003/2004 | Financial year 2002/2003 |
|---------------------------|--------------------------|--------------------------|
| Value as of 01.10.        | 3,856                    | 3,537                    |
| Addition                  | 3,818                    | 3,190                    |
| Reversal                  | (149)                    | (141)                    |
| Utilisation               | (2,770)                  | (2,526)                  |
| Currency effects          | (113)                    | (204)                    |
| <b>Value as of 30.09.</b> | <b>4,642</b>             | <b>3,856</b>             |

## (12) Other current liabilities

Other current liabilities are comprised as follows:

| € '000                                  | 30.09.2004   | 30.09.2003   |
|---|--------------|--------------|
| Liabilities from taxation               | 677          | 232          |
| Liabilities from social security        | 435          | 388          |
| Liabilities from value-added tax claims | 413          | -            |
| Other liabilities                       | 422          | 520          |
| <b>Other current liabilities</b>        | <b>1,947</b> | <b>1,140</b> |

## (13) Pension obligations

The rollforward of the projected benefit obligations are shown in the following table:

| € '000   | Financial year 2003/2004 | Financial year 2002/2003 |
|--|--------------------------|--------------------------|
| Pension benefit obligation at the beginning of the financial year  | 923                      | 550                      |
| Service cost   | 100                      | 94                       |
| Interest cost  | 56                       | 33                       |
| Actuarial gain/loss  | 412                      | 206                      |
| Asset transfer   | (4)                      | 40                       |
| Benefits paid  | (1)                      | -                        |
| <b>Pension benefit obligation at the end of the financial year</b> | <b>1,486</b>             | <b>923</b>               |

The funded status – the difference between the projected benefit obligation and the fair value of plan assets – is reconciled with the provisions shown on the balance sheet as shown below:

| € '000  | 30.09.2004   | 30.09.2003 |
|---|--------------|------------|
| Funded status   | 1,486        | 923        |
| Unrecognised net (gain) or loss                                 | (679)        | (279)      |
| Unrecognised prior service cost                                 | -            | -          |
| <b>Unfunded accrued benefit cost</b>                            | <b>807</b>   | <b>644</b> |
| Additional minimum liability                                    | 463          | -          |
| <b>Provisions for pensions (Accumulated benefit obligation)</b> | <b>1,270</b> | <b>644</b> |

The additional minimum liability amounted to € 463,000 at 30 September 2004 and is recognised as a component of *Other comprehensive loss* without affecting net income.

| € '000   | Financial year 2003/2004 | Financial year 2002/2003 |
|--|--------------------------|--------------------------|
| Increase in minimum liability included in Other comprehensive loss | 463                      | -                        |

Pension expenditure is as follows:

| € '000  | Financial year 2003/2004 | Financial year 2002/2003 |
|---|--------------------------|--------------------------|
| Wages and salaries                                  | 100                      | 94                       |
| Interest expenses for projected benefit obligations | 56                       | 33                       |
| Amortisation fo actuarial gains/losses              | 11                       | 1                        |
| <b>Pension expenditure</b>                          | <b>167</b>               | <b>128</b>               |

The Company does not fund its pension obligations.

The following assumptions were used to determine benefit obligations:

| in %                                    | Financial year 2003/2004 | Financial year 2002/2003 |
|---|--------------------------|--------------------------|
| Discount rate                           | 5.5                      | 6.0                      |
| Rate of long-term compensation increase | 3.0                      | 2.5                      |
| Rate of long-term pension increase      | 1.0                      | 1.0                      |

The annual pension increase was 1.75% in the financial year 2003/2004 and 1.5% in the previous year. The pension calculation considers employee turnover. 65 was taken as the basic pensionable age.

**Estimated future pension benefit payments**

Pension benefits pertaining to the Group's plan were € 1,000 respectively during 2003/2004 and € 0 respectively during 2002/2003. The total estimated future pension benefits to be paid by the Group's pension plans for the next 10 years approximate € 74,000 and are expected to be paid as follows:

| Financial year as of 30.09. (€ '000) | Pension benefit payments |
|--------------------------------------|--------------------------|
| 2005                                 | 1                        |
| 2006                                 | 2                        |
| 2007                                 | 3                        |
| 2008                                 | 5                        |
| 2009                                 | 6                        |
| 2010-2014                            | 57                       |

**(14) Long-term debt**

The long-term debt is comprised as follows:

| € '000   | 30.09.2004   | 30.09.2003   |
|--|--------------|--------------|
| Annuity loan, repayable in quarterly instalments of € 123,719 including interest, term 18 years, interest rate of 6.24% fixed for 10 years | 4,842        | 5,028        |
| <b>Total long-term debt</b>  | <b>4,842</b> | <b>5,028</b> |
| Less current portion of long-term debt   | 198          | 187          |
| <b>Long-term debt, net of current portion</b>  | <b>4,644</b> | <b>4,841</b> |

As of 30 September 2004 the Company's long-term liabilities have the following contractual maturities:

| Financial year as of 30.09. (€ '000) | Liabilities  |
|--------------------------------------|--------------|
| 2005                                 | 198          |
| 2006                                 | 211          |
| 2007                                 | 225          |
| 2008                                 | 239          |
| 2009                                 | 254          |
| Thereafter                           | 3,715        |
| <b>Total long-term liabilities</b>   | <b>4,842</b> |

Borrowings have been secured to the full amount by mortgages.

## (15) Public subsidies

The Company received subsidies from various public bodies within the framework of state economic development programmes. These subsidies related to the construction of manufacturing facilities, research and development activities, advanced training programmes and interest subsidies. The grants disclosed in the consolidated financial statements in hand for the years ending 30 September 2004 and 2003 are as follows:

| € '000   | Financial year 2003/2004 | Financial year 2002/2003 |
|--|--------------------------|--------------------------|
| Research and development subsidies   | 977                      | 1,790                    |
| Other subsidies  | 224                      | 302                      |
| <b>Total</b>   | <b>1,201</b>             | <b>2,092</b>             |
| Investment grants set off from acquisition costs for property, plant and equipment | 224                      | 158                      |

## (16) Financial instruments and risk provisioning

The market value of a financial instrument is estimated as the amount that could be obtained under current market conditions between an independent buyer and seller.

The Company is of the opinion that the credit risk for these types of transaction is negligible.

The market values were calculated on the basis of market conditions on the balance sheet date – interest rates, currency rates, commodity prices – by the evaluation methods described below. The market values of derivative instruments are calculated independently of and do not consider movements in the fair value of underlying transactions that are economically hedged by these instruments.

Financial assets and liabilities whose book values approximate market value include cash and cash equivalents, short-term financial assets, trade accounts receivable and payable and other short-term liabilities.

The market value of debt or similar long-term liabilities is the present value of cash flows anticipated in the future. The discount rate is based on applicable interest rates (for comparable loans to borrowers with similar credit standing) as of the balance sheet date.

The market value of forward currency contracts is calculated on the basis of the average spot exchange rate as of the balance sheet date, adjusted for forward premiums and discounts for the respective residual term of the contract, as compared to the contracted forward exchange rate.

In the case of currency options, acknowledged models were used to determine the option price. In addition to the residual term, the market value of an option is also influenced by other factors, e.g. the current level and volatility of the underlying base lending or exchange rate.

As of 30 September 2004 the Company had currency forward contracts with a total nominal value of € 2.294 million (previous year: € 1.150 million).

The following table shows the book values and estimated market values of the financing instruments as of 30 September 2004 and 30 September 2003.

| € '000                                   | 30.09.2004 |              | 30.09.2003 |              |
|--|------------|--------------|------------|--------------|
|  | Book value | Market value | Book value | Market value |
| Originated financial instruments         |            |              |            |              |
| Assets                                   |            |              |            |              |
| Trade accounts receivable                | 26,243     | 26,243       | 30,344     | 30,344       |
| Accounts receivable affiliated companies | 35,915     | 35,915       | 20,451     | 20,451       |
| Loans                                    | 2,871      | 2,871        | 2,818      | 2,818        |
| Cash and cash equivalents                | 49,748     | 49,748       | 45,015     | 45,015       |
| Liabilities                              |            |              |            |              |
| Trade accounts payable                   | 10,592     | 10,592       | 10,636     | 10,636       |
| Accounts payable affiliated companies    | 5,072      | 5,072        | 5,919      | 5,919        |
| Loans                                    | 4,842      | 5,187        | 5,028      | 5,028        |
| Leasing commitments                      | 23,431     | 24,734       | 25,105     | 26,107       |
| Derivative financial instruments         |            |              |            |              |
| Assets                                   |            |              |            |              |
| Currency hedging contracts               | 141        | 141          | 436        | 436          |
| Liabilities                              |            |              |            |              |
| Currency hedging contracts               | -          | -            | -          | -            |

## (17) Contingent liabilities and other financial obligations

### Leases and rental agreements

The Company leases office space, land and equipment under leasing and rental agreements which may not be cancelled during the basic term. Lease and rental expenses for the financial years 2003/2004 and 2002/2003 amounted to € 1.923 million and € 2.355 million respectively.

The future minimum rental and leasing payments on the basis of non-cancellable lease and rental agreements are:

| Financial year (€ '000)       | Leasing and rental agreements |
|-------------------------------|-------------------------------|
| 2004/2005                     | 1,427                         |
| 2005/2006                     | 1,258                         |
| 2006/2007                     | 662                           |
| 2007/2008                     | 35                            |
| 2008/2009                     | 28                            |
| <b>Total minimum payments</b> | <b>3,410</b>                  |

### Sale-and-lease-back

On 28 September 1999 the Company sold land, building and leasehold improvements in Dublin for approx. € 34.081 million and simultaneously entered into a long-term leasing agreement for this same property. This sale-and-lease-back arrangement is a financial lease in accordance with SFAS No. 98 "Accounting for Leases" whereby the land, buildings and leasehold improvements continue to be carried and depreciated on the lessee's books. The leasing agreement has a term of 20 years.

The following table shows the minimum lease payments to be made each year for the land, building and leasehold improvements. In the financial years 2003/2004 and 2002/2003 € 2.118 million (US\$ 2.613 million) and € 2.418 million (US\$ 2.613 million) were paid respectively.

| € '000                                   | Leasing payments |
|--|------------------|
| Leasing liabilities                      |                  |
| 2004/2005                                | 2,393            |
| 2005/2006                                | 2,393            |
| 2006/2007                                | 2,393            |
| 2007/2008                                | 2,393            |
| 2008/2009                                | 2,393            |
| From 2009/2010                           | 28,802           |
| <b>Total leasing liabilities</b>         | <b>40,767</b>    |
| Minus interest                           | (17,336)         |
| <b>Net leasing liabilities</b>           | <b>23,431</b>    |
| Less current portion                     | (656)            |
| <b>Long-term net leasing liabilities</b> | <b>22,775</b>    |

**Guarantees**

There are guarantees towards third parties amounting to € 223,000.

Generally, these guarantees represent standby letters of credit to banks related to services provided to customers and from suppliers.

No provision in compliance with FIN 45 was formed for these guarantees, since a payment obligation is not likely to occur.

**Purchase commitments**

Carl Zeiss Meditec has purchase commitments towards suppliers amounting to € 30.461 million. These are distributed over several years.

**Litigation**

The Group has reached an out-of-court settlement in the action for damages against I-Spire s.p.r.l., Brussels/Belgium and its sole proprietor in the financial year 2003/2004. I-Spire s.p.r.l. had acquired some of the assets and liabilities of the former Asclepion-Meditec marketing partner Icon Laser Eye Centers, Inc., of Toronto, Canada within the scope of an asset deal. The action, which was initiated by Carl Zeiss Meditec, involved claims for damages for breach of contract, outstanding debts and the repayment of loans. The lawsuit related to the overall balance sheet item "Other loans" totalling € 2.818 million, although the sum involved was in excess of this amount. The appropriate adjustments had already been made on "Other loans" in the financial year 2001/2002. This settlement provides for the payment of the total amount shown in the balance sheet item "Loans" by I-Spire s.p.r.l. in accordance with a payment plan. The first instalment of € 1.500 million was paid at the end of April 2004 and a further payment of € 0.250 million was made subsequent to the balance sheet date in October 2004. Inasmuch, any possible risks may be considered as having been eliminated to the greatest-possible degree.

Current litigation risks arise from the lawsuit and claim for lost earnings filed by a distributor of the former Asclepion for dermatological lasers, and the pending cost reimbursement lawsuit and claim filed by the insolvency administrator of the former Asclepion distribution partner U.S. Medical, Inc., also in the field of dermatological lasers. The Company has taken adequate precautionary measures for both law suits.

## (18) Stock option plan

With the resolution adopted by Asclepion's extraordinary general meeting on 10 March 2000 the Management Board was authorised, subject to the approval of the Supervisory Board, to issue 400,000 option rights. The following conditions were applicable to the issue and exercising of the rights:

- The Management Board and the employees of the Company are eligible to subscribe.
- The recipients must be employed by a member company of the Carl Zeiss Meditec Group at the time the rights are issued.

Of the 400,000 options authorised approximately 300,000 were issued to existing employees (those employed on 5 June 2000). The remaining 100,000 options were issued to persons who entered into the employment of the Carl Zeiss Meditec Group through to 1 October 2003. The purchase price for the existing employees is the issue price of € 29 of Asclepion-Meditec AG; in the case of options issued thereafter the purchase price will be the average of the Xetra closing prices on the five stock exchange trading days before and after the options are granted minus a discount of 30%. The initial options granted were exercisable in three tranches: up to one third of the options received may be exercised following the publication of the half-year report 2001/2002, up to two thirds following the publication of the half-year report 2002/2003, and all the options after the publication of the half-year report 2004/2005. Analogous regulations are applicable to the new employees. However, options may only be exercised if the reference price for Carl Zeiss Meditec shares for the first tranche has increased by at least 30% over the issue price (for new employees: the granting price). A 45% increase is required for the second tranche and a 60% increase for the third tranche. The reference price is the average of the Xetra closing prices on the five stock exchange trading days before and after the publication of the respective half-year report.

The following shows the Company's stock options as of 30 September 2004 and 2003.

|   | Financial year 2003/2004 |                             | Financial year 2002/2003 |                             |
|---|--------------------------|-----------------------------|--------------------------|-----------------------------|
|   | Number of options        | Average exercise price in € | Number of options        | Average exercise price in € |
| Outstanding options at the beginning of the financial year  | 108,700                  | 28.33                       | 241,360                  | 26.91                       |
| Granted (Total)   | -                        | -                           | -                        | -                           |
| Existing employees  | -                        | -                           | -                        | -                           |
| New employees   | -                        | -                           | -                        | -                           |
| Terminated (Total)  | (3,200)                  | 29.00                       | (132,660)                | -                           |
| Existing employees  | (3,200)                  | 29.00                       | (105,160)                | 29.00                       |
| New employees   | -                        | -                           | (27,500)                 | 13.31                       |
| Exercised   | -                        | -                           | -                        | -                           |
| <b>Outstanding options at the end of the financial year</b> | <b>105,500</b>           | <b>28.31</b>                | <b>108,700</b>           | <b>28.33</b>                |

The status of the stock options as of 30 September 2004 is as follows:

| Issued  |   |
|---|---|
| Average fair value of the options granted in the course of the year (per option) in € | - |
| Exercisable   |   |
| Number of options   | - |
| Average exercise price in €   | - |

The Company has not posted any remuneration expenses pursuant to APB No. 25 since during all periods presented, the intrinsic value of the awards was zero. This was due to the fact that the exercise hurdle on none of the options was exceeded.

The average fair value of the options granted during the year (per option) is divided among the employees as follows: (Figures for existing employees, new employees I and II relate to the options issued in the financial year 2000. New employees III–VI relate to the quarters of the financial year 2001):

| in €               | Fair value per option in € |
|--------------------|----------------------------|
| Existing employees | 16.26                      |
| New employees I    | 25.00                      |
| New employees II   | 21.35                      |
| New employees III  | 16.26                      |
| New employees IV   | 9.79                       |

The entire fair value of options granted in the financial year was € 54,000, using a Black/Scholes option price model with the following assumptions:

|   |         |
|---|---------|
| Expected volatility for stock options issued in FY 2000     | 69.70%  |
| Expected volatility for stock options issued in FY 2001     | 99.30%  |
| Expected dividend return                                    | 0%      |
| Risk-free interest rate for stock options issued in FY 2000 | 4.83%   |
| Risk-free interest rate for stock options issued in FY 2001 | 3.90%   |
| Expected term   | 4 years |

The fair value of the options granted in the financial year ending on 30 September 2004 was calculated on the assumption that approx. 30% of the granted options would lapse before the necessary vesting conditions would be achieved.

The risk-free interest rate was set in accordance with the current yield for German treasury bonds (*Bundesanleihen*) with a term of 3-5 years.

The volatility assumption was based upon a study of a peer group. This peer group comprises various companies on the US market. The companies concerned belong to the same industry as Carl Zeiss Meditec. The volatilities of the peer group in the past 4 years, which corresponds to the expected term of the options, and the volatility of the Company's own shares, have been included in the above volatility calculation at a weighting of 50 % each. The Company believes that the result approximates the expected future volatility over the assumed lives of the options.

## **(19) Employee participation program**

In the financial year 2003/2004 it was resolved to issue 25 free shares to each employee of Carl Zeiss Meditec AG and its wholly-owned subsidiaries with the exception of the Management Board of Carl Zeiss Meditec AG, the President of Carl Zeiss Meditec Inc., Dublin, USA, as well as the managing directors of the wholly-owned subsidiaries. The Company's purchased own shares shall be used to service the compensatory stock plan (see note 20).

This resulted in personnel expenses valued at € 323,000 in the financial year 2003/2004.

## **(20) Equity**

### **Treasury stock**

With resolution of the annual meeting of shareholders on 12 March 2003, Carl Zeiss Meditec was authorised to acquire own shares up to a value corresponding to 10% of the share capital of € 25.833 million until 11 September 2004.

As of 30 September 2003 a total of 14,252 shares had been purchased at an average price of € 7.58 per share and reported as "Treasury stock" under shareholders' equity.

With resolution of the annual meeting of shareholders on 19 March 2004, Carl Zeiss Meditec was authorised to acquire own shares up to a value corresponding to 10% of the share capital of € 28.417 million until 18 September 2005.

Based on this new resolution, in the financial year 2003/2004 an additional 6,923 shares have been purchased at an average price of € 10.19 per share and reported as described above.

**Cash capital increase in the financial year 2002/2003**

On 18 September 2003 Carl Zeiss Meditec effected a capital increase. A total of 2,583,329 new no-par value bearer shares were tendered by public offering in Germany and international private placement at a subscription price of € 9.70 per share. After issue expenses of € 430,000 had been subtracted from the gross proceeds of € 25.058 million, the net cash inflow to Carl Zeiss Meditec from the capital increase amounted to € 24.628 million.

The cash capital increase was recorded in the commercial register at the domicile of Carl Zeiss Meditec on 25 September 2003.

The share capital of Carl Zeiss Meditec had thus increased by € 2.584 million from € 25.833 million to € 28.417 million. The capital reserve increased accordingly by € 22.044 million to € 89.433 million.

By resolution of the listing committee of the Frankfurt securities exchange dated 25 September 2003, the new shares were admitted to the regulated market and to a subsection of the regulated market subject to additional admission criteria (Prime Standard). Such shares were included in stock exchange dealings on the regulated market on 29 September 2003.

**Other comprehensive loss not affecting net income**

The following table shows the movement of the components of other comprehensive loss:

| € '000  | Financial year 2003/2004 | Financial year 2002/2003 |
|---|--------------------------|--------------------------|
| Difference arising from currency conversion     |                          |                          |
| Change in unrealised translation gains/(losses) | (2,071)                  | (5,007)                  |
| Increase in minimum liability                   | (270)                    | -                        |
| <b>Change in other comprehensive loss</b>       | <b>(2,341)</b>           | <b>(5,007)</b>           |

Under the German Stock Corporation Act (*Aktiengesetz*), the amount of dividends available for distribution to the shareholders is dependent upon the equity of Carl Zeiss Meditec AG reported in its financial statements in accordance with the German Commercial Code. Dividends may only be declared and paid from possible retained earnings (after transfer to statutory reserves) as posted in the Company's annual German statutory financial statements. Such amounts differ from the total retained earnings as shown in the accompanying financial statements prepared in accordance with US GAAP. As of 30 September 2004, the German statutory financial statements of Carl Zeiss Meditec AG posted accumulated earnings of € 13.073 million.

## (21) Shares of outside shareholders

The shares of outside shareholders relate to the investment in Carl Zeiss Meditec Co., Ltd., Japan. The Company purchased 51% of the shares of Carl Zeiss Meditec Co., Ltd., Japan in the financial year 2002/2003 and controls this entity. Carl Zeiss Co., Ltd., Japan, is the remaining minority shareholder and owns both common and preferred shares in Carl Zeiss Meditec Co., Ltd., Japan. Due to Carl Zeiss Co., Ltd.'s ownership of preferred shares, Carl Zeiss Co., Ltd. will receive 66 % of the future dividend payments from Carl Zeiss Meditec Co., Ltd., Japan for at least three financial years following the acquisition date. The preferred shares were conveyed for advance services performed by Carl Zeiss Co., Ltd. in the field of marketing, establishment of a service structure and support for the approval procedures of Carl Zeiss Meditec products.

## (22) Taxes on income and earnings

Income (loss) before income taxes is attributable to the following geographic regions:

| € '000  | Financial year 2003/2004 | Financial year 2002/2003 |
|---------|--------------------------|--------------------------|
| Germany | 3,839                    | (3,123)                  |
| Abroad  | 21,254                   | 19,837                   |
|         | 25,093                   | 16,714                   |

Taxes on income and earnings are as follows:

| € '000          | Financial year 2003/2004 | Financial year 2002/2003 |
|-----------------|--------------------------|--------------------------|
| Current taxes:  |                          |                          |
| Germany         | 630                      | 284                      |
| Abroad          | 7,713                    | 9,401                    |
|                 | 8,343                    | 9,685                    |
| Deferred taxes: |                          |                          |
| Germany         | 1,674                    | (1,207)                  |
| Abroad          | (205)                    | (1,202)                  |
|                 | 1,469                    | (2,409)                  |
|                 | 9,812                    | 7,276                    |

Since 1 January 2001 a uniform tax rate has been applied for taxing the income of joint stock corporations under German corporate tax law (*Körperschaftsteuergesetz*). In accordance with the tax law applicable in the financial year 2003/2004, the Company's income was subject to a corporate tax rate of 25% plus a solidarity surcharge of 5.5% on corporate tax. The total tax rate including solidarity surcharge amounts to 26.4%. The law stipulating a one-time increase in corporation tax to 26.5% for the calendar year 2003 was announced in September 2002. The majority of German companies are subject to two types of income tax, a) trade earnings tax and b) corporation tax. The trade earnings tax of the Company in Jena amounted to 15.97 % for each of the financial years 2003/2004 and 2002/2003. Trade taxes are deductible for the purpose of computing corporate income taxes. Together with trade tax of 15.97% the Company's tax burden in the financial year 2003/2004 totalled 38.13%, in the financial year 2002/2003 39.46%.

The expected income tax benefit (expense), based on income (loss) before income taxes of € 25.093 million and € 16.714 million and statutory rates of 38.13% in the financial year 2003/2004 and 39.46% in the financial year 2002/2003 to actual income tax expense is as follows:

| € '000   | Financial year 2003/2004 | Financial year 2002/2003 |
|--|--------------------------|--------------------------|
| Expected tax expense at statutory rate               | 9,568                    | 6,595                    |
| Increase in deferred tax assets valuation adjustment | -                        | 566                      |
| Non-deductible expenses                              | 559                      | 69                       |
| Tax-exempt earnings                                  | (799)                    | (938)                    |
| Effect of change in statutory tax rate               | 196                      | 759                      |
| Other  | 288                      | 225                      |
| <b>Taxes on income</b>                               | <b>9,812</b>             | <b>7,276</b>             |
| Thereof from continuing operations                   | 9,812                    | 9,014                    |
| Thereof from discontinued operations                 | -                        | (1,738)                  |
| Effective taxation ratio                             | 39.10%                   | 43.53%                   |

Deferred tax assets and liabilities are made up of the following:

| € '000                        | 30.09.2004 | 30.09.2003 |
|-------------------------------|------------|------------|
| Loss carryforward             | 7,513      | 9,126      |
| Property, plant and equipment | 4,634      | 4,471      |
| Accounts receivable           | 602        | 1,077      |
| Provisions                    | 2,408      | 2,110      |
| Inventories                   | 3,990      | 4,340      |
| Deferred revenue              | 62         | -          |
| Other current assets          | 320        | 220        |
| Other non-current assets      | 58         | 70         |
| Loans                         | 1,049      | 2,097      |
| Accounts payable              | 275        | 406        |
| Deferred tax assets           | 20,911     | 23,917     |
| Valuation adjustment          | 1,861      | 2,588      |
| Deferred tax assets net       | 19,050     | 21,329     |
| Property, plant and equipment | 279        | 295        |
| Intangible assets             | 1,860      | 1,937      |
| Other assets                  | 24         | 10         |
| Accounts payable              | 71         | 82         |
| Deferred tax liabilities      | 2,234      | 2,324      |
| Deferred tax assets (net)     | 16,816     | 19,005     |

Deferred tax assets and liabilities were disclosed in the consolidated balance sheet as of 30 September 2004 and 2003 as follows:

| € '000                                | 30.09.2004 | 30.09.2003 |
|---------------------------------------|------------|------------|
| Deferred tax assets, current          | 7,419      | 7,958      |
| Deferred tax assets, non-current      | 10,063     | 11,281     |
| Deferred tax liabilities, current     | 108        | 8          |
| Deferred tax liabilities, non-current | 563        | 226        |
|                                       | 16,816     | 19,005     |

Deferred tax liabilities on the retained earnings of foreign subsidiaries to the sum of € 1.133 million and non-deductible expenses for retained earnings of foreign subsidiaries to the sum of € 14.114 million were not carried as a liability because these earnings are to remain permanently invested.

The consolidated financial statements of the Company in the financial year 2003/2004 carried a valuation discount of € 1.861 million for deferred taxes. This valuation allowance reduced the deferred tax asset to a net amount which the Company believes more likely than not that it would realise, based on the Company's estimate of future earnings and the expected timing of temporary difference reversals. As of 30 September 2004 the Company had a tax credit of € 7.513 million from loss carryforwards, of which about € 867,000 can be carried forward to 2020, € 421,000 to 2021 and € 6.225 million treated as unlimited carryforwards. These carryforwards relate to activities in the USA and Germany.

### (23) Segment information

According to SFAS 131 "Disclosures about Segments of an Enterprise and Related Information", segment reporting follows the internal organisational and reporting structure of the Group.

Therefore, the segment reporting is based on the geographical regions Germany, USA, Japan and other corresponding with the locations. Each segment offers the same type of products and services.

| € '000                              | Financial year 2003/2004 |          |          |        |              |              |
|-------------------------------------|--------------------------|----------|----------|--------|--------------|--------------|
|                                     | Germany                  | USA      | Japan    | Others | Eliminations | Consolidated |
| Sales revenues                      | 110,721                  | 136,926  | 35,302   | -      | (48,071)     | 234,878      |
| Cost of goods sold                  | (73,487)                 | (80,608) | (19,125) | -      | 47,343       | (125,877)    |
| Selling and marketing expenses      | (17,053)                 | (22,246) | (8,013)  | -      | 189          | (47,123)     |
| General and administrative expenses | (6,825)                  | (3,835)  | (1,094)  | (64)   | 119          | (11,699)     |
| Research and development expenses   | (10,605)                 | (14,785) | -        | -      | 493          | (24,897)     |
| Other expenses                      | 15                       | 204      | -        | 19     | 14           | 252          |
| Foreign currency gains/losses       | 474                      | -        | 61       | -      | 257          | 792          |
| Operating income/loss               | 3,240                    | 15,656   | 7,131    | (45)   | 344          | 26,326       |
| Long-term assets                    | 11,186                   | 18,111   | 195      | -      | (2,551)      | 26,941       |
| Depreciation                        | 2,808                    | 2,631    | 66       | -      | (31)         | 5,474        |
| Interest expenses                   | 465                      | 1,790    | 57       | 1      | (124)        | 2,189        |
| Capital expenditure                 | 787                      | 2,021    | 57       | -      | (40)         | 2,825        |
| Goodwill                            | 15,422                   | 704      | -        | -      | -            | 16,126       |
| Balance sheet total                 | 239,811                  | 80,838   | 14,672   | 12     | (119,900)    | 215,433      |

€ '000

Financial year 2003/2004

|                                     | Germany  | USA      | Japan    | Others | Eliminations | Consolidated |
|-------------------------------------|----------|----------|----------|--------|--------------|--------------|
| Sales                               | 96,686   | 148,456  | 31,851   | 717    | (41,996)     | 235,714      |
| Cost of goods sold                  | (60,602) | (95,131) | (16,114) | (707)  | 39,370       | (133,184)    |
| Selling and marketing expenses      | (15,573) | (22,009) | (5,644)  | (609)  | 272          | (43,563)     |
| General and administrative expenses | (5,235)  | (3,260)  | (2,531)  | (116)  | 30           | (11,112)     |
| Research and development expenses   | (9,917)  | (13,443) | -        | (4)    | 466          | (22,898)     |
| Other expenses                      | 253      | 630      | -        | 795    | (1,159)      | 519          |
| Foreign currency gains/losses       | (601)    | (43)     | 113      | (1)    | (221)        | (753)        |
| Operating income/loss               | 5,011    | 15,200   | 7,675    | 75     | (3,238)      | 24,723       |
| Long-term assets                    | 14,071   | 18,063   | 222      | -      | (3,538)      | 28,818       |
| Depreciation                        | 2,673    | 2,927    | 55       | 19     | (24)         | 5,650        |
| Interest expenses                   | 507      | 2,051    | 47       | 84     | (127)        | 2,562        |
| Capital expenditure                 | 899      | 1,744    | 277      | -      | (130)        | 2,790        |
| Goodwill                            | 10,373   | 743      | -        | -      | -            | 11,116       |
| Balance sheet total                 | 232,678  | 84,145   | 14,346   | 532    | (125,856)    | 205,845      |

Sales revenue is allocated according to the geographic region of the subsidiary that generates the revenue. Long-term assets comprise long-term tangible assets and loans, but not goodwill, intangible assets, long-term accounts receivable or deferred tax assets.

Inter-segmental sales and revenue are largely calculated at the same prices as negotiated with outsiders to the Group.

Capital expenditure relates to the purchase of property, plant and equipment.

**Geographical information**

Revenues from external customers are attributed to geographical regions based on the location of the customer.

| € '000                        | Financial year 2003/2004 | Financial year 2002/2003 |
|-------------------------------|--------------------------|--------------------------|
| Germany                       | 17,734                   | 16,393                   |
| Abroad                        |                          |                          |
| Europe, not including Germany | 41,860                   | 40,051                   |
| Americas                      | 109,806                  | 123,490                  |
| Asia, Pacific region*         | 65,478                   | 55,780                   |
|                               | 234,878                  | 235,714                  |

\* including Africa

**Sales by business segment**

| € '000      | Financial year 2003/2004 | Financial year 2002/2003 |
|-------------|--------------------------|--------------------------|
| Diagnostics | 169,798                  | 178,826                  |
| Laser       | 44,102                   | 34,527                   |
| Service     | 20,978                   | 22,361                   |
|             | 234,878                  | 235,714                  |

**Information on major customers**

In the financial years 2003/2004 and 2002/2003 no single customer accounted for more than 10% of total sales.

**(24) Transactions subject to reporting requirements during the period**

The following is a summary of securities transactions carried out by members of the Management and Supervisory Boards in the financial year 2003/2004 that were subject to reporting requirements pursuant to Art. 15a of the German Securities Trading Act (*WpHG*).

| Name                    | Function                                 | Date       | Purchase/sale | Number of shares | Price   |
|-------------------------|--|------------|---------------|------------------|---------|
| Alexander von Witzleben | Deputy Chairman of the Supervisory Board | 10.09.2004 | Sale          | 1,000            | € 10.20 |
| Alexander von Witzleben | Deputy Chairman of the Supervisory Board | 15.04.2004 | Sale          | 1,000            | € 11.70 |
| Dr Michael Kaschke      | Chairman of the Supervisory Board        | 03.05.2004 | Purchase      | 250              | € 10.60 |
| Dr Michael Kaschke      | Chairman of the Supervisory Board        | 03.05.2004 | Purchase      | 250              | € 10.70 |

## (25) Events after the balance sheet date

Carl Zeiss Meditec, Inc. and the US company Laser Diagnostic Technologies, Inc. (LDT), based in San Diego, Calif., announced that on 20 October 2004 they signed a definitive agreement for the acquisition of LDT by Carl Zeiss Meditec. LDT developed and commercialised a new standard for glaucoma detection with its proprietary ocular nerve fiber measurement instrument. Worldwide sales of approximately US-\$ 20 million with a break-even operating result are expected for the current financial year.

The transaction is expected to close at the end of 2004, pending the requisite company and shareholder approvals.

On 1 November 2004 the Company also announced that its Japanese subsidiary, Carl Zeiss Meditec Co., Ltd., domiciled in Tokyo, Japan, was taking over the surgery business of Carl Zeiss Co., Ltd., which is also domiciled in Tokyo, Japan. This area deals with the sale of surgical microscopes for ophthalmology, neurosurgery and for ear, nose and throat surgery, and achieves annual sales of ca. € 25 million.

This is a transaction under common control, as all companies are controlled by Carl Zeiss AG. Goodwill is not created by this transaction. US GAAP requires that the residual amount of € 1.258 million paid in excess of the respective book values of the acquired assets and liabilities be offset against equity.

## Specific comments and compulsory disclosures

### in conformance with Art. 292a *HGB*

#### Divergent accounting, valuation and consolidation methods

The consolidated financial statements of Carl Zeiss Meditec were prepared in accordance with Art. 292a *HGB* and considering the exemption for *HGB* consolidated financial statements in compliance with the valid American accounting principles, US GAAP, as of the balance-sheet date.

In conformity with the interpretation of the German Accounting Standards Committee (DRSC) in DRS 1 the consolidated reporting of the parent company complies with Directive 83/349/EEC.

The applied accounting, valuation and consolidation methods in accordance with US GAAP essentially differ in the following respects:

#### Balance sheet layout

The balance sheet and the income statement for the German annual financial statements was laid out in accordance with Art. 266, 275 *HGB*. SEC/ US GAAP prescribes a different layout: The balance sheet items are ordered in accordance with their realisability – beginning with the most liquid items. Furthermore, short-term components of the long-term assets and liabilities are posted separately. Treasury stock was not shown as an asset, but openly deducted on the liabilities side under Shareholders' equity.

#### Self-constructed software

According to *HGB* self-constructed software must not be posted on the balance sheet, but the resulting costs are to be disclosed immediately as expenses.

Under US GAAP expenses for software developments may be capitalised in accordance with SFAS No. 86 "Accounting for the Costs of Computer Software to Be Sold, Leased or Otherwise Marketed" and depreciated over the probable useful life. Once feasibility has been proven, the development costs for software (attributable material and labour costs and overheads) for sale to third parties from the time of technical feasibility to market maturity are to be capitalised.

**Business combinations**

According to German accounting rules, business combinations must be taken into consideration as of their effective date. A choice may be made between the book value method and the fair value (Art. 301 *HGB*). By the book value method capital is carried at an amount equal to the book value of the assets to be included in the consolidated financial statements. Hidden reserves may only be disclosed to the amount of the differential between the book value of participations and the calculated equity capital. By the revaluation method hidden reserves are disclosed independently of the proportional holding.

According to US GAAP the date the merger was recorded in the commercial register is the date on which the acquisition is recorded. The fair value of the assets and liabilities associated with the legal transferee at the time of acquisition must be recorded.

**Goodwill**

Starting 1 October 2002 the Company has adjusted its financial records to conform to SFAS No. 142, "*Goodwill and Intangible Assets*" which prohibits the recognition of scheduled depreciation on goodwill. According to this regulation the current value of goodwill is periodically assessed and it is written off at a lower value as necessary. *HGB* stipulates that goodwill be amortised over the anticipated useful life.

**Uncompleted development projects at acquisitions**

In conformity with *HGB*, expenses for uncompleted development projects at acquired subsidiaries are not recognised separately, but as a constituent part of goodwill. According to US GAAP, these costs are identified separately at the date of acquisition and disclosed as expenses.

**Leasing**

According to US accounting standards there is a fundamental difference between "capital lease" and "operating lease". In the case of a capital lease, the lessee is the economic owner and capitalises the leased property. In the case of an operating lease, the leased property is attributed to the lessor and the lessee makes periodic rental payments to use the property.

There are special regulations for posting sale-and-lease-back agreements. The profit from the sale of the equipment is deferred and amortised to income pro rata over the term of the agreement.

**Unrealised profit/loss within the framework of valuation on the effective date**

Under *HGB* only unrealised losses are reported in the income statement (impairity principle). US GAAP, on the other hand, also takes into account any unrealised profit, particularly related to the measurement of derivative financial instruments.

Accounts receivable and liabilities denominated in foreign currencies and which are not hedged are valued under German accounting legislation at cost price or the lower exchange rate on the balance sheet date. Under American accounting standards (SFAS No. 52) all foreign currency accounts receivable and liabilities are translated at the exchange rate on the reporting date and unrealised exchange rate gains and losses reflected in the operating results.

The valuation of derivative financial instruments pursuant to *HGB* takes into account the principles of cost price, realisation and imparity.

Under US GAAP financial instruments are stated at their market value. Any resulting unrealised profit or loss is reflected in the results.

**Deferred taxes**

Pursuant to *HGB*, deferred taxes are calculated for all different timing differences between the recognition of income for tax purposes and for the consolidated income statement (timing concept). No deferred taxes are shown for losses carried forward. However, DRS 10, Deferred taxes in consolidated financial statements, requires that losses carried forward for financial years beginning after 31 December 2002 be disclosed if the tax advantage can be realised with a reasonable degree of certainty.

Pursuant to SFAS No. 109, however, deferred taxes must be calculated for all temporary differences between the tax bases of assets and liabilities and the respective amounts reported in the consolidated balance sheet (temporary concept). Deferred taxes on loss carryforwards are to be recognised. In this respect, the future rate of taxation is also applied if the rate has been enacted.

Valuation allowances are provided against deferred tax assets when realisation of such assets is not more likely than not.

### **Provisions for pensions**

Pursuant to both *HGB* and US GAAP provisions must be made for pension obligations. The value to be recorded under US GAAP is to be based on anticipated discounted future payments. Pursuant to *HGB*, various insurance mathematical methods may be used. According to US GAAP the projected unit credit method must be applied (SFAS No. 87). Pursuant to SFAS No. 87, in the case of schemes financed by means of funds, certain qualified assets must be offset against the total obligation or capitalised.

### **Employee participation program**

In accordance with US GAAP there are two alternatives for the valuation of option awards granted to employees. Under APB No. 25 the intrinsic value of the award, as determined on the measurement date, is recorded as an expense over the vesting period of the option award. Alternatively, SFAS 123 may be applied. Under this method, the fair value of the options is determined with the aid of a valuation method (e.g. Black/Scholes option price model) and expensed over the period through to when the options are vested. The Company applies APB 25 to the consolidated financial statements. The pro forma result, had SFAS 123 been applied, is disclosed in the notes.

According to *HGB* there are no expenses for stock option plans from contingent capital.

### **Outside interests in shareholders' equity**

Pursuant to *HGB*, shares held by outside investors are disclosed according to the entity theory of consolidation as a component part of shareholders' equity and the net result for the year. In accordance with US accounting rules, shares held by outside investors are according to the parent company theory not shown as a component part of shareholders' equity, but as a separate balance sheet item after shareholders' equity and the share of profits apportioned to the minorities disclosed as an expense or, in the case of a deficit, as income in the income statement.

## Other mandatory disclosures pursuant to Art. 292a Commercial Code (*HGB*)

### Details on executive bodies of the parent company

#### Management Board

The following persons were appointed to the Management Board of Carl Zeiss Meditec AG in the financial year 2003/2004 and their names recorded in the commercial register:

· **Ulrich Krauss, Dipl.-Kaufmann (MBA), Weimar**

President and CEO, responsible for Sales, Marketing, Service, HR, Refractive Surgery and Business Development, as of 1 October 2004 also responsible for Quality and Product Management, Research and Development.

*Other mandates:*

Member of the Board of Carl Zeiss Meditec Inc., Dublin, USA

Member of the Board of Carl Zeiss Meditec, Co. Ltd., Tokyo, Japan

· **Bernd Hirsch, Dipl.-Kaufmann (MBA), Weimar**

Member of the Management Board, responsible for Finances, Investor Relations, IT and Legal Affairs, since 1 October 2004 also responsible for Logistics and Production, Research and Development.

*Other mandates:*

Managing Director of AM Asset Management GmbH, Jena

Member of the Board of Carl Zeiss Meditec, Co. Ltd., Tokyo, Japan

· **Dr. Walter-Gerhard Wrobel, Physicist, Jena (until 30 September 2004)**

Member of the Management Board, responsible for Logistics and Production, Research and Development, Quality and Product Management.

The active members of the Management Board received a total remuneration of € 668,000 for the financial year 2003/2004.

## Supervisory Board

The Supervisory Board of Carl Zeiss Meditec AG in the financial year 2003/2004 consisted of the following members:

### · **Dr. Michael Kaschke, Oberkochen**

Member of the Management Board of the Carl Zeiss AG, Oberkochen

Chairman of the Supervisory Board

*Other mandates:*

Chairman of the Board of Carl Zeiss Meditec Inc., Dublin, USA,

Chairman of the Board of Carl Zeiss Optical, Inc., Chester, USA,

Chairman of the Board of Carl Zeiss Australia Pty. Ltd., Camperdown, Australia,

Chairman of the Board of Carl Zeiss Co. Ltd., Tokyo, Japan,

Chairman of the Board of Carl Zeiss Surgical, Inc., Thornwood, USA,

Chairman of the Board of Carl Zeiss Pte. Ltd., Singapore,

Chairman of the Board of Carl Zeiss India Pte. Ltd., Singapore,

Chairman of the Board of Carl Zeiss Co. Ltd., Seoul, South Korea,

Chairman of the Board of Carl Zeiss Far East Co., Ltd., Kowloon, Hongkong,

Chairman of the Board of Carl Zeiss (Pty.) Ltd., Randburg, South Africa,

Chairman of the Supervisory Board of Carl Zeiss Financial Services GmbH, Oberkochen,

Member of the Supervisory Board of Carl Zeiss Semiconductor Manufacturing Technologies AG, Oberkochen,

Member of the Supervisory Board of Hensoldt AG, Wetzlar,

Member of the Supervisory Board of Siltronic AG, Munich,

Chairman of SPECTARIS, the German Industrial Association for Optical, Medical and Mechatronical Technologies, Berlin.

### · **Alexander von Witzleben, Weimar**

Chairman of the Management Board of Jenoptik AG, Jena,

Deputy Chairman of the Supervisory Board

*Other mandates:*

Chairman of the Supervisory Board of Analytik Jena AG, Jena,

Chairman of the Supervisory Board of Meissner+Wurst Zander Holding AG, Stuttgart,

Chairman of the Supervisory Board of PVA Tepla AG, Asslar,

Chairman of the Supervisory Board of DEWB AG, Jena,

Member of the Supervisory Board of Krone GmbH, Berlin,

Member of the Administrative Board of Feintool International Holding AG, Lyss.

· **Dr. Franz-Ferdinand von Falkenhausen, Jena**

Managing Director of Carl Zeiss Jena GmbH, Jena  
Member of the Supervisory Board. (until 30 September 2004)

*Other mandates:*

Member of the Supervisory Board of Carl Zeiss Semiconductor Manufacturing Technologies AG, Oberkochen,  
Member of the Supervisory Board of FC Carl Zeiss Jena, Jena,  
President of the IHK (Chamber of Commerce) East Thuringia, Gera,  
Chairman of the Board of Trustees of the Fraunhofer Institute (IOF), Jena,  
Member of the Board of Trustees of Innovent Jena e.V., Jena,  
Chairman of the Advisory Board of the Thüringer Aufbaubank, Erfurt,  
Member of the Advisory Board of ZSP Geodätische System GmbH, Jena (Trimble Group),  
Member of the Advisory Board of AJZ Engineering GmbH, Jena,  
Member of the Advisory Board "East" of Dresdner Bank AG,  
Member of the Advisory Board "East" of Deutsche Bank AG,  
Member of the Advisory Board of Ernst-Abbe-Stiftung,  
Member of the State Board of Trustees Saxony-Anhalt/Thuringia of the Founders' Association for German Science,  
Member of the Board of Trustees of the Jena Polytechnic College.

· **Dr. Manfred Fritsch, Kleinpürschütz bei Jena**

Member of the Supervisory Board

*Other mandates:*

Member of the Supervisory Board of Messe AG, Erfurt,  
Member of the Board of the Kompetenznetz Optische Technologie OptoNet e.V., Jena,  
Chairman of the Advisory Board Verkehrslandeplatz Schöngleina GmbH, Schöngleina.

· **Dr. Markus Guthoff, Krefeld**

Member of the Board of the IKB Deutsche Industriebank AG, Düsseldorf  
Member of the Supervisory Board (since 1 October 2004)

*Other mandates:*

Chairman of the Advisory Board of IKT Private Equity GmbH, Düsseldorf,  
Chairman of the Advisory Board of IKB Data GmbH, Düsseldorf,  
Member of the Supervisory Board of MetaDesign AG, Berlin,  
Member of the Supervisory Board of Argantis GmbH, Cologne,  
Member of the Advisory Board of Poppe & Potthoff, Werther,  
Member of the Board of IKB Capital Corporation, New York, USA.

· **Wilhelm Burmeister, Jena**

Group Manager Manufacturing Control and Chairman of the Works Council of Carl Zeiss Meditec AG, Jena  
Member of the Supervisory Board on behalf of the employees (since 1 October 2004)

*no other mandates.*

· **Jürgen Dömel, Jena**

Chairman of the Group Works Council at Carl Zeiss AG, Oberkochen  
Chairman of the Works Council at Carl Zeiss Jena GmbH, Jena,  
Member of the Supervisory Board on behalf of the employees (until 30 September 2004)

*Other mandates:*

Member of the Supervisory Board of Carl Zeiss Jena GmbH, Jena  
Member of the Supervisory Board of Carl Zeiss AG, Oberkochen

· **Franz-Jörg Stündel, Jena**

Service Technician at Carl Zeiss Meditec AG, Jena,  
member of the works council of Carl Zeiss Meditec AG, Jena  
Member of the Supervisory Board on behalf of the employees

*no other mandates.*

The active members of the Supervisory Board received a total remuneration of € 130,000 for the financial year 2003/2004. The amount of fixed and variable remuneration of individual members of the Supervisory Board is calculated in compliance with the Company's articles of association.

**Advances/loans and contingent liabilities in favour of members of executive bodies**

No advances or loans have been granted to members of the executive bodies. The Company has not entered into any contingent liabilities in favour of members of the Management Board/Supervisory Board.

**Personnel expenses**

Personnel expenses for the financial years 2003/2004 and 2002/2003 were as follows:

| € '000                   | Financial year 2003/2004 | Financial year 2002/2003 |
|--------------------------|--------------------------|--------------------------|
| Wages and salaries       | 54,569                   | 55,586                   |
| Social security expenses | 5,860                    | 5,909                    |
|                          | 60,429                   | 61,495                   |

The expenses for employee pensions amounted to € 1.388 million and € 1.395 million in the financial years 2003/2004 and 2002/2003 respectively.

As of the cut-off date 30 September 2004 the number of staff was 796 (previous year: 752) plus 23 trainees (previous year: 24). The annual average of Company employees was 801 (previous year: 798).

**Cost of materials**

The cost of materials for the financial years 2003/2004 and 2002/2003 comprised the following:

| € '000                     | Financial year 2003/2004 | Financial year 2002/2003 |
|----------------------------|--------------------------|--------------------------|
| Raw materials and supplies | 82,615                   | 90,026                   |
| Purchased services         | 13,524                   | 16,772                   |
|                            | 96,139                   | 106,798                  |

**Details on shareholdings (fully consolidated companies)**

| Name and domicile of the company                                  | Currency  | Share of voting capital % | Shareholders' equity as of 30.09.2004 translated at the market rate on the balance sheet date | thereof profit/loss for financial year 2003/2004 at average annual rate |
|---|-----------|---------------------------|---|---|
| Carl Zeiss Meditec, Inc.,<br>Dublin, USA                          | US\$ '000 | 100                       | 39,337  | 11,619  |
|   | € '000    |                           | 31,883  | 9,555   |
| Asclepion-Meditec, S.R.L.i.L.,<br>Milan, Italy *                  | € '000    | 100                       | 12  | (46)  |
| AM Asset Management<br>Verwaltungsgesellschaft mbH, Jena, Germany | € '000    | 100                       | (262)   | 14  |
| Carl Zeiss Meditec Systems GmbH, Pirmasens                        | € '000    | 100                       | 327   | (71)  |
| Carl Zeiss Meditec Co., Ltd.<br>Tokyo, Japan                      | ¥ '000    | 51                        | 1,158,356   | 532,464   |
|   | € '000    |                           | 8,456   | 4,047   |

\*The figures relate to the liquidation balance sheet as of 31 March 2004

**German Corporate Governance Code / Declaration according to Art. 161 (Stock Corporation Act)**

The declaration mandated under Art. 161 German Stock Corporation Act (AktG) was made available to the Management and Supervisory Boards and the shareholders.

Jena, 22 November 2004

Carl Zeiss Meditec AG



**Ulrich Krauss**  
President and CEO



**Bernd Hirsch**  
Member of the Management Board

## Audit opinion

We have audited the consolidated financial statements, comprising the balance sheet, income statement and the statement of changes in shareholders' equity and cash flows as well as the notes to the financial statements, prepared by Carl Zeiss Meditec AG, for the financial year from 1 October 2003 to 30 September 2004. The preparation and the content of the consolidated financial statements are the responsibility of the Company's Management Board. Our responsibility is to express an opinion whether the consolidated financial statements are in accordance with United States Generally Accepted Accounting Principles (US GAAP).

We conducted our audit of the consolidated financial statements in accordance with German auditing regulations and generally accepted standards for the audit of financial statements promulgated by Institut der Wirtschaftsprüfer (IDW, German Institute of Auditors). Those standards require that we plan and perform the audit such that it can be assessed with reasonable assurance whether the consolidated financial statements are free of material misstatements. Knowledge of the business activities and the economic and legal environment of the Group and evaluations of possible misstatements are taken into account in the determination of audit procedures. The evidence supporting the amounts and disclosures in the consolidated financial statements are examined on a test basis within the framework of the audit. The audit includes assessing the accounting principles used and significant estimates made by the management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements provide a suitable understanding of the net assets, financial position and results of operations as well as cash flows of the Group for the financial year in compliance with United States Generally Accepted Accounting Principles.

Our audit, which also extends to the consolidated management report prepared by the Management Board for the financial year from 1 October 2003 to 30 September 2004, did not lead to any reservations. The consolidated management report provides a suitable understanding of the Company's position and suitably presents the risks of future development.

In addition, we confirm that the consolidated financial statements and the consolidated management report for the financial year from 1 October 2003 to 30 September 2004 satisfy the conditions required for Company's exemption from its obligation to prepare consolidated financial statements and the group management report in accordance with German law.

Stuttgart, 24 November 2004

Prof. Dr. Binder, Dr. Dr. Hillebrecht & Partner GmbH  
Wirtschaftsprüfungsgesellschaft  
Steuerberatungsgesellschaft



**Schupeck**  
Wirtschaftsprüfer



**Barth**  
Wirtschaftsprüfer