Sunshine Heart, Inc.

Innovative Therapy for Treating Heart Failure

Sunshine Heart • Annual Report 2008

Sunshine Heart is a global medical device company, committed to the commercialisation of the C-Pulse™, an implantable, non-blood contacting, heart assist device for the treatment of people with heart failure. These patients include a large and under-served potential market segment and provide a significant market opportunity for the Company.

Contents

Notice of Meeting

The Annual General Meeting of Sunshine Heart, Inc. will be held at the offices of Henry Davis York, 44 Martin Place, Sydney on Thursday 30 October 2008 at 12 noon.

Chairman's Letter

Dear Shareholders,

Annual General Meeting

You are invited to attend the 2008 Annual General Meeting to be held in Sydney on Thursday 30 October, 2008. A notice of meeting is enclosed together with the Company's 2008 annual report.

Milestones achieved

It has been a further year of progress for Sunshine Heart, both in the United States and at St Leonards (Sydney) in development of the C-Pulse™ heart assist device. The major areas of activity include:

- Negotiations with the US Food and Drug Administration (FDA) in regard to the Company's Investigational Device Exemption (IDE) application to commence a US clinical trial;
- Substantial completion of the C-Pulse driver development. The first clinical production units for use in the US IDE trial have been built, tested and shipped by our design partner Plexus;
- Manufacture of other components including a new percutaneous line;
- Further training of surgical and clinical teams at our 6 US university affiliated clinical trial sites; and
- Completion of an underwritten $5.4 million rights issue.

IDE application

The C-Pulse is designed to relieve (and in some cases reverse) the symptoms of moderate to severe heart failure through the use of counterpulsation technology which generates an increase in cardiac output, an increase in coronary blood flow and a reduction in the heart's pumping workload.

Whilst C-Pulse is simple to describe, it is a complex and innovative medical device. We have had extensive communications with the FDA over the past year in regard to the design of the proposed clinical trial and the manufacture, operation and reliability of the C-Pulse device. Considerable documentation and testing has been generated in support of the application. The process has been robust and useful and we remain optimistic that the company will be granted approval to commence the US clinical trial during 2008.

Medical community support

The current treatment regimes for sufferers of moderate heart failure are drugs and CRT pacemakers. Approximately two thirds of patients with moderate heart failure do not respond in a material way to this treatment regime. C-Pulse has the potential to provide symptom relief to this large group.

We are encouraged by the interest that C-Pulse is generating in the global medical community and specifically, the United States. This last year, C-Pulse was featured at major meetings in the US including the Heart Failure Society of America, the Northwestern University Heart Failure Symposium and the International Society for Heart and Lung Transplantation.

The Company has previously identified 6 university affiliated medical institutions to enrol patients into the clinical trial and has undertaken training for both surgical and clinical personnel from these institutions. It is pleasing to report that these institutions remain very enthusiastic about their participation in the trial, when approved.

Funding

During the year, the Company raised $11.4 million comprising $6.0 million from the final tranche of the September 2006 equity raising and $5.4 million from a 4 for 11 rights issue offered to all shareholders which was underwritten by major shareholders GBS Venture Partners and CM Capital. We express our appreciation to those shareholders who participated in the rights issue and to the underwriters for their continued support. With a cash balance of almost $10 million at 30 June 2008, the Company is well positioned to commence the US clinical trial, when approved. The Company expects to raise additional equity in 2009.

Changes to the Board

In July 2008, we announced the appointment of Nicholas Callinan to the board. Nick's experience in technology development and global venture capital will be of considerable value to the company. His appointment is to be ratified by resolution at the annual general meeting. At the same time, Dr Conrad Wang retired from the board and we thank him for his contribution.

I will be standing down as Chairman at the annual general meeting, the fourth anniversary of the Company's stock exchange listing. Nick Callinan has accepted appointment as Chairman and a resolution relating to Nick's appointment is included in the notice of meeting. I have been invited by the board to serve as a non-executive director, a role I am pleased to accept.

I would like to express the board's appreciation to the management team and staff for their work, insight and effort during the year. In particular, I would like to thank CEO Donald Rohrbaugh for his continued leadership, Medical Director and co-founder Dr William Peters and COO Victor Windeyer. We also thank the technology team at St Leonards and the regulatory affairs team for their considerable effort in managing the IDE process. They are a small, productive and gifted group of design, clinical and regulatory specialists who can deliver the C-Pulse product to market.

Yours sincerely

Malcolm McComas
Chairman
21 August 2008

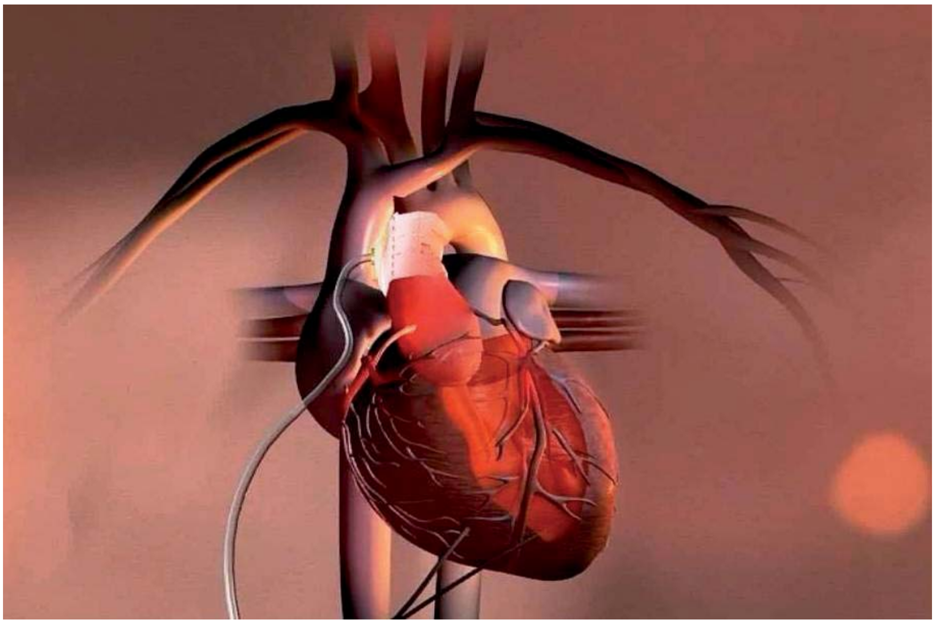
Chief Executive Officer's Review

Dear Shareholders,

During the past year we expected to receive US Food and Drug Administration (FDA) approval to undertake a US clinical trial of our heart assist device C-Pulse™, whilst approval has not yet been received, we have interacted extensively with the FDA and remain optimistic that approval to start a US clinical trial will be received by year end. C-Pulse is designed to relieve (and in some cases reverse) the symptoms of moderate heart failure, a debilitating condition whereby patients suffer shortness of breath, tiredness, swelling of legs and ankles, and fatigue with minimal exertion such as walking. Left untreated, heart failure normally leads to increased hospitalisations and premature death.

Sufferers of moderate heart failure do not respond to the currently approved drug treatment regime and in some cases, patients with electrical disorders who are treated with cardiac resynchronization therapy (CRT) pacemakers also do not respond. In the US alone, there are approximately one million sufferers of moderate heart failure (1 in 300 US residents) who await a therapy to relieve their symptoms and improve their quality of life.

In moderate heart failure, the heart has lost some 30 – 40% of its capacity to pump blood around the body. C-Pulse through the use of counterpulsation technology is able to increase cardiac output, increase coronary blood flow and reduce the heart's pumping workload. Importantly the C-Pulse Cuff, as shown in the illustration below, is on the exterior of the ascending aorta and is thus positioned outside of the blood system. Hence there are minimal risks of blood clots and strokes. Blood thinning medication is not required.



C-Pulse Cuff on exterior of ascending aorta

C-Pulse is expected to be the first heart assist system for moderate heart failure in an FDA approved clinical study.

In addition, C-Pulse is expected to be the first non-blood contacting heart assist therapy in an FDA approved clinical study.

The Sunshine Heart team has worked diligently this past year and is well prepared to take the next crucial steps with C-Pulse. In reflecting upon this year's progress and successes, the phrase "readiness for 2009" comes to mind. This "readiness" can be grouped into five areas:

- Readiness for the US IDE clinical trial
- Readiness for clinical use of the C-Pulse System
- Readiness for market and medical community awareness
- Readiness for advancing the fully implanted C-Pulse
- Readiness for assurance of financial stability.

US IDE clinical trial readiness

Our path to approval has involved extensive dialogue and meetings with the FDA and with our clinical sites. Mary Beth Kepler, Director of Clinical and Regulatory Affairs, provides key dialog and interface with the FDA and also manages the US clinical team. William Peters, MD, continues to lead all clinical efforts as our Chief Medical Officer with prime focus on the clinical protocols. Victor Windeyer, COO and the St. Leonard's engineering team focus on providing all test validation and documentation for the C-Pulse System.

Training continues with the six US clinical site's study teams in conjunction with Alquest, Inc., our study Clinical Research Organization which has a vast network of resources and experience in developing and conducting clinical trials.

We have also established the FDA-required independent medical review teams to provide clinical study oversight including the Data Safety Monitoring Board (DSMB), Clinical Events Committee (CEC) and Core Laboratories. These teams will be positioned to assure consistency and accuracy of patient data. The clinical results will be independently monitored by the DSMB and CEC, which are led respectively by experienced cardiologists, Drs. Jay Cohn and Sidney Goldstein. Dr. Cohn is a renowned heart failure researcher and speaker who founded the Heart Failure Society of America in 1994.

Contractual relationships are progressing with all the university based clinical sites and they await FDA approval to begin the Institutional Review Board (IRB) process. As shown in the map opposite Sunshine Heart's clinical sites are located in the areas of high incidence of heart failure to help ensure patient enrolment in the trial.

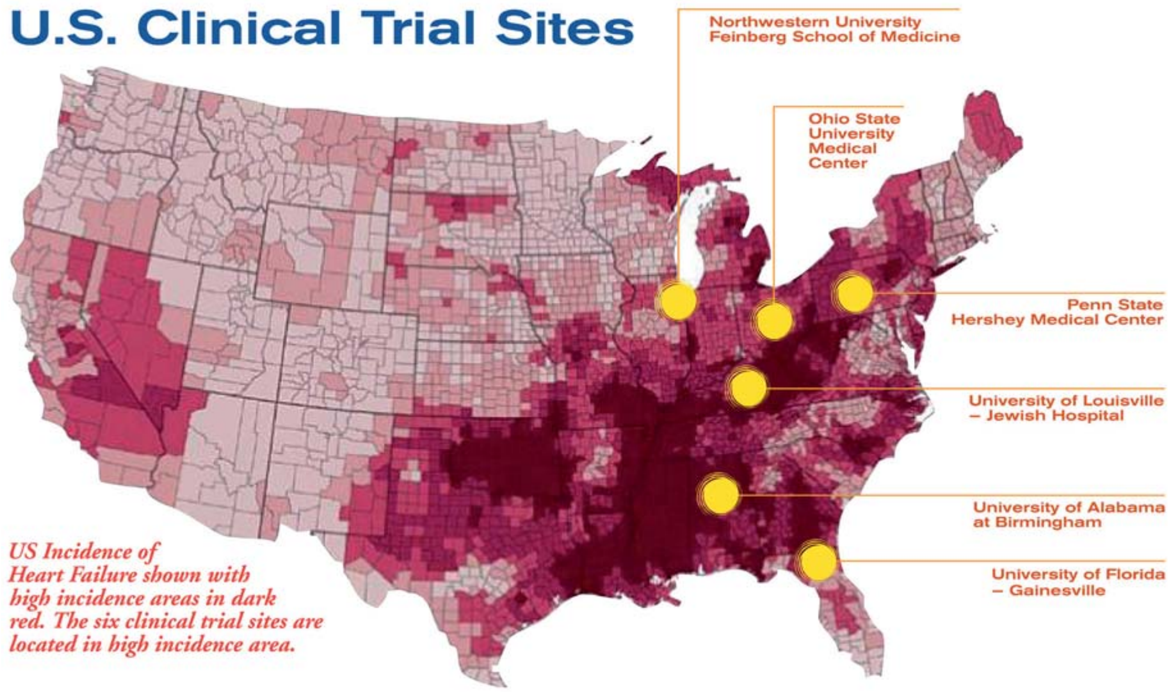
C-Pulse system clinical readiness

The Sunshine Heart engineering team has worked diligently to complete additional testing to strengthen our IDE submission data, based upon feedback from the FDA and to increase System performance. Most importantly, on-going durability tests on the implanted portion of the C-Pulse, the Cuff, confirm that reliability goals have been met and exceeded. We are pleased to report that Cuffs have now exceeded seven years of equivalent life, which is three years greater than our goal. Clinical design units have been produced and the C-Pulse system is ready for the rigorous demands of clinical use.

Market and medical community awareness

Interest from the medical community continues to build as clinicians in the United States become more aware of C-Pulse. C-Pulse was included in heart assist therapy presentations made by US physicians at two major professional meetings: Heart Failure Society of America and the Northwestern University Heart Failure Symposium. Additionally, clinical results from the Australian and New Zealand (ANZ) study were presented at two major medical meetings: the International Society of Heart and Lung Transplantation in Boston and the Cardiac Society of Australia and New Zealand in Christchurch.

In addition to the clinical interest, the US media featured C-Pulse in a front-page article in the Medical Device Daily. We also boosted our media presence with a new web-site www.sunshineheart.com that includes C-Pulse animation and interviews with our co-national principal investigators, Drs. Patrick McCarthy and William Abraham.



Readiness to advance the fully implanted C-Pulse

The Company's long term goal is to develop a fully implanted C-Pulse system. Considerable progress was made during 2008 with the completion of specifications and design requirements for the fully implanted system. The design uses the same aortic Cuff configuration that has been successfully used clinically in the ANZ study and will be used in the US clinical trial. However rather than the Cuff being inflated by an external driver, a small implanted driver is being developed. The driver will be powered by a transcutaneous energy transfer system from an external power supply, similar to other implanted systems. It should be noted that since C-Pulse is non-blood contacting and does not have to operate at all times, the criticality of the energy transfer system is greatly diminished and thus there is no need for an implanted power backup system (internal battery) required by other implanted heart support systems.

Financial stability assurance

In November 2007 the Company received the final proceeds ($6 million) of its staged $20 million fund raising announced in September 2006. Subsequently in May 2008 the Company undertook a pro rata rights issue to all shareholders to raise $5.4 million. The rights issue was fully underwritten by Sunshine Heart's major shareholders GBS Venture Partners and CM Capital and supported by many current shareholders. We greatly appreciate the continued support of underwriters and shareholders. Further fund raising will be required to complete the necessary clinical studies for commercialisation of C-Pulse. Additionally the Company expects to receive reimbursement of part of the clinical trial costs from US heath insurance companies.

2008 foundation for 2009 major achievements

Building upon the 2008 foundation, Sunshine Heart anticipates FDA approval of the clinical trial during the remainder of 2008 and then subsequent enrolment of patients at the above mentioned six medical institutions. Based on our experience with clinical trials in Australia and New Zealand we are very confident of outstanding patient outcomes from the US trial. At the same time the Company will continue to focus on the development of a fully implantable C-Pulse.

Summary

With the progress achieved in 2008, we are ready to move C-Pulse into the US clinical trial environment during 2009. In the US alone, more than 5.3 million people suffer from heart failure, a progressive disease with treatment costs exceeding $34.8 billion annually. Among these patients, more than 1.4 million have progressed to moderate heart failure indicated by the presence of shortness-of-breath and fatigue during mild exercise (such as walking). With the aging of baby boomers and the progressive nature of heart failure, significant growth in the incidence of moderate heart failure is expected. Specifically targeted for the treatment of moderate heart failure, Sunshine Heart's C-Pulse therapy offers an earlier treatment for patients with improvement in quality of life and prevention from further degradation of their condition. I want to personally thank you for your continued interest and support of Sunshine Heart. I also offer my sincere thanks and appreciation to the total Sunshine Heart team who continue to move us closer to our goal.

Yours sincerely

D.G. Rohrbaugh

Donald Rohrbaugh
Chief Executive Officer
21 August 2008

Directors

The names and details of the company's directors in office during the financial year and until the date of this report are as follows. Directors were in office for this entire period unless otherwise stated.

Names, qualifications, experience and special responsibilities

Mr Malcolm McComas BEc LLB SF Fin FAICD (Non-executive Chairman)

Mr McComas became a director and the chairman of Sunshine Heart on 20 July 2004. He is a member of the Audit, Compliance and Corporate Governance Committee.

Mr McComas has 24 years investment banking experience and 5 years legal experience. He has experience in equity and debt finance, acquisitions and divestments, and the structuring and implementation of major equity issues and privatisations.

Since 1999, he has been a director and is now a consultant to Grant Samuel, the corporate advisory, property services and funds management group. In the previous 10 years, he established and developed County NatWest's corporate finance business which in 1998 became, through merger, the investment banking division of Salomon Smith Barney in Australia (a subsidiary of Citigroup, Inc). Mr McComas was a managing director and co head of investment banking at Salomon Smith Barney and managing director of investment banking at County NatWest.

Mr McComas has a Bachelor of Economics and a Bachelor of Laws from Monash University. He is a Senior Fellow and a National Council Member of the Financial Services Institute of Australia. During the past 3 years Mr McComas has served as a director of Pharmaxis Limited, a listed entity.

Mr John Brennan LLB

Mr Brennan became a non-executive director of Sunshine Heart on 1 November 2006. He is a member of the Remuneration and Nomination Committee.

Mr Brennan is a Partner of CM Capital Investments, an Australian venture capital fund manager. CM Capital Investments manages $260 million in early stage venture capital funds focused on the life sciences and telecommunications sectors. Mr Brennan has more than 15 years of venture capital, corporate finance, commercial and legal experience. Prior to joining CM Capital in 2004, Mr Brennan had experience in mergers and acquisitions, divestments, capital raisings, venture capital and private equity gained from corporate and advisory roles both internationally and in Australia. Mr Brennan started his career as a corporate and commercial lawyer in Brisbane. He subsequently gained international experience in the UK where he worked for GE Capital and Ernst & Young Corporate Finance in M&A and corporate finance roles. At GE Capital Mr Brennan had a pan European M&A role focused on acquisitions, strategic equity investments and divestments for one of its main operating businesses. Mr Brennan holds a Bachelor of Laws degree from Queensland University of Technology.

Dr Geoff Brooke MBBS MBA
Dr Brooke became a director of Sunshine Heart on 25 September 2003. He is the Chairman of the Remuneration and Nomination Committee.

Dr Brooke is managing director of GBS Venture Partners Limited and the manager of $400 million in early staged venture funds. With more than 15 years of venture capital experience, Dr Brooke has been a founder, lead investor and director of many healthcare and bioscience based companies in the US and Australia, a number of which have been sold or undertaken IPO's on either NASDAQ or ASX. A medical graduate of the University of Melbourne with five years of clinical experience, Dr Brooke holds an MBA from IMEDE (now IMD) in Switzerland. During the past 3 years Dr Brooke has served as a director of the following other listed companies:

- Cogstate Limited
- ChemGenex Pharmaceuticals Ltd *

Mr Nicholas Callinan BE MBA (appointed 10 July 2008)
Mr Callinan is the founder and managing partner of Collins Hill Pty Ltd which provides advice to institutional investors and funds managers in the global private equity and venture capital markets where he has worked for over 20 years in several countries including the UK and USA. In the early 1990's he set up investment funds in the former communist countries of Central Europe. Previously in the early 1980's he was founder and chief executive of the Advent group of companies which were one of the first venture capital investment groups in Australia. He has served on a number of company boards both private and public, government bodies and charitable foundations in Australia and overseas. He has degrees in Engineering and Business Administration from the University of Melbourne.

Dr Richard Lin MD (resigned 15 November 2007)
Dr Lin became a director of Sunshine Heart in December 2002 and was a member of the Remuneration and Nomination Committee until his resignation on 15 November 2007.

Dr Lin is a Partner at Three Arch Partners, a Silicon Valley-based venture capital firm specialising in funding the development of medical technologies, healthcare services, biotechnology, and information technology. Prior to joining Three Arch Partners, he received his general surgical training at the University of California, San Francisco. He also spent time as a research scientist at the University of California, San Francisco, School of Medicine and Harvard Medical School.

Mr Crispin Marsh BSc FAICD
Mr Marsh became a non-executive director of Sunshine Heart on 1 July 2006 and a member of the Audit Committee on 17 July 2008. He was the executive director of Corporate Affairs of Sunshine Heart, until 30 June 2006. He has been associated with Sunshine Heart since its inception in 1999, having been the inaugural Chairman of the company. Mr Marsh has been responsible within Sunshine Heart for administration, legal issues, intellectual property protection, obtaining research grants, contract negotiation and management of corporate relationships.

Mr Marsh is also managing director of SCP Technology and Growth Pty Ltd, an independent innovation commercialisation consultancy. He has been directly involved in the successful commercialisation of a number of technologies in a variety of technical fields including the medical area. It was in this role that he co-founded Sunshine Heart with Dr Peters.

An Australian patent attorney since 1969, Mr Marsh was a partner of an Australian firm of patent attorneys for nearly 30 years before establishing SCP. He has a BSc degree from the University of Sydney, is a registered mediator and a Fellow of the Australian Institute of Company Directors. Mr Marsh is a director of Australian Biotechnology and Healthcare Fund No. 3 Ltd.

* *denotes current directorship*

Mr Donal O'Dwyer BE MBA

Mr O'Dwyer became a non-executive director of Sunshine Heart in July 2004. He is the Chairman of the Audit, Compliance and Corporate Governance Committee.

Mr O'Dwyer relocated to Australia in 2004, having retired as Worldwide President of Cordis Cardiology, the cardiology division of a Johnson & Johnson subsidiary, Cordis Corporation. In this role Mr O'Dwyer saw Cordis Cardiology move from number four to number one in market share of coronary stents worldwide. Prior to joining Cordis he worked 12 years for Baxter Healthcare, rising from plant manager in Ireland to president of the Cardiovascular Group, Europe. He brings a wealth of medical device experience to Sunshine Heart. During the past three years Mr O'Dwyer has also served as a director of the following other listed companies:

- Cochlear Limited *
- Mesoblast Limited *
- AtCor Medical Holdings Limited *

Dr William Peters MBChB MD (Medical Director and Chief Technical Officer)

Dr Peters is responsible for implementing the clinical trials and defining the device development appropriate for the clinical need. Dr Peters is the inventor of the C Pulse and was co founder and start up CEO of Sunshine Heart. He has served as a member of the Board since inception.

Dr Peters has a track record of successful invention and commercialisation in the field of cardiac technologies. He previously invented a system for endovascular cardiopulmonary bypass to allow minimally invasive cardiac surgery. This technology was assigned to Heartport, Inc, which listed on NASDAQ in 1996 and was bought by Johnson & Johnson in 1999. Dr Peters spent 2 years as a research fellow in minimally invasive cardiac surgery (1994-1995) at Stanford University, California. He was also employed during this time as manager of medical affairs at Heartport, Inc. Dr Peters completed a medical degree at Otago University 1989 and a Doctorate of Medicine (MD) at Monash University in 2002. Dr Peters has a strong interest in devices to support the failing heart, and has clinical experience in thoracic transplantation and use of various LVADs (including Biomedicus, Abiomed, Thoratec, Novacor and IAB systems). Dr Peters has authored or co-authored over 20 published articles and 4 book chapters regarding cardiac surgery.

Dr Peters' continued association with heart surgery, as a research fellow in cardiothoracic surgery at Auckland City Hospital, affords Sunshine Heart a direct view of developments in the heart surgery field generally, and in the field of congestive heart failure in particular.

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* *denotes current directorship*

Mr Donald Rohrbaugh MSME (Director and Chief Executive Officer)

Mr Rohrbaugh joined Sunshine Heart in September 2002 as a consultant. Mr Rohrbaugh became the CEO and was appointed to the board in January 2003 and is responsible for implementing the Company's strategies and tactics approved by the Board of Directors.

Previously, Mr Rohrbaugh was the founding CEO and director of Acorn Cardiovascular, Inc., a company engaged in developing a non-active device treatment for heart failure. During Mr Rohrbaugh's role as President and Chief Executive Officer, from December 1997 to December 2001, Acorn completed 4 rounds of financing totalling $US47.6 million to advance the innovative Cardiac Support Device, CorCap, from concept to Phase II randomised clinical trials in the USA and Europe.

Mr Rohrbaugh has also served as a consultant to various venture capital firms. At times he served as CEO for start-up companies such as Embolix, which was acquired by Edwards Lifesciences, eMED Corporation and AMED Systems. In those roles he also served on the Board of Directors.

From 1977 to 1996, Mr Rohrbaugh held a variety of executive management positions with Baxter Healthcare International, including Vice President of Research and Development for the Edwards Critical Care Division and Vice President/General Manager of the Edwards MDS and the Novacor Division (an LVAD manufacturer).

Mr Rohrbaugh has over 30 years of business and product development experience in both the domestic and international medical device markets, including nearly 15 years with heart failure devices. He also has 10 years experience in the scientific instrumentation business and 4 years in the aerospace field.

Mr Rohrbaugh's formal education includes a Bachelor of Science in Mechanical Engineering from Pennsylvania University and a Master of Science in Mechanical Engineering from University of Southern California.

Dr Conrad Wang MD BS MBA (appointed 15 November 2007, resigned 10 July 2008)

Dr Wang is an associate of Three Arch Partners, a Silicon Valley-based venture capital firm specialising in funding the development of medical technologies, healthcare services, biotechnology, and information technology. Prior to joining Three Arch Partners, he completed his medical and orthopaedic training at the Harvard Medical School where he also spent time as a research scientist. Dr Wang also holds an MBA from Harvard Business School and a Bachelor of Science in Mechanical Engineering from Massachusetts Institute of Technology.

Company Secretary

Mr Brian Bolton BCom MBA FCPA

Mr Bolton is the Chief Financial Officer and Company Secretary of Sunshine Heart since he joined the Company in April 2007. Mr Bolton is responsible for all financial, taxation, compliance (non-clinical), risk and company secretarial functions.

Mr Bolton has held various financial and treasury executive positions with Esso Australia Ltd during his 16 year tenure in both Australia and the USA. In addition he has 12 years of experience as Chief Financial Officer with ASX listed Plutonic Resources Ltd and Atlantic Gold NL.

Directors' Interests

The direct and indirect interests of the directors in the shares of the Company (including interest in options) are set out in note 20. There has been no change in director's interests post year end.

Earnings per Share

Basic Earnings per Share	(4.8) cents
Diluted Earnings per Share	(4.8) cents.

Dividends

No dividends were paid or recommended to be paid during the year (2007: Nil).

Corporate Information

Corporate structure

Sunshine Heart, Inc. is a company limited by shares that is incorporated in Delaware, USA. It has prepared a consolidated financial report incorporating the entity that it controlled during the financial year, Sunshine Heart Company Pty Limited.

Nature of operations and principal activities

The principal activity during the year of entities within the consolidated entity was the design and development of heart assist devices.

There have been no significant changes in the nature of those activities during the year.

Employees and Consultants

The consolidated entity employed 13 employees and 5 consultants as at 30 June 2008 (2007: 12 employees and 4 consultants).

Operational and Financial Review

Group Overview

The Company has continued the development of the C-Pulse heart assist device during the year including activities to support an IDE trial in the United States.

Operating Results for the Year

The Group incurred a net loss for the year of $9,738,183 (2007 loss - $11,539,413). The level of expenditure was less than the prior year due to lower C-Pulse development costs and a stronger Australian dollar.

Likely Developments and Expected Results

Over the coming year, Sunshine Heart's efforts shall focus on the following key areas:

- Seeking US FDA approval to commence a US clinical trial; and
- Completing design specification on the next generation fully implantable C-Pulse device.

The Company expects to make an operating loss for the 2009 financial year. The Company's business plan necessitates continued spending in pursuit of the business objectives. The Company's ongoing success will depend on its continued ability to raise additional capital in the future.

Cash Used in Operations

Net cash flows used in operating activities was $9,151,862 (2007: $9,997,492).

Liquidity and Funding

The Company has sufficient funds to commence its C-Pulse clinical trial following FDA approval, however, further funding will be required in order to commericialise C-Pulse.

Significant Events After Balance Date

There were no material events occurring after balance date which may affect either the Group's operations or results of those operations or the Group's state of affairs.

Share Options

Unissued shares

As at the date of this report, there were 63,499,423 options over unissued ordinary shares in Sunshine Heart, Inc.

Employee Options

During the year ended 30 June 2008, a total of 691,000 options over unissued ordinary shares were issued as remuneration to consultants and employees of the Company. During the year 7,605,858 options were cancelled or forfeited including 6,446,000 options where performance milestones were not achieved.

Placement Options

During the year ended 30 June 2008, a total of 16,000,000 options over unissued ordinary shares were issued as part of tranche 2 of the capital raising.

Refer to note 12(c) of the financial statements for further details of the options outstanding.

Option holders do not have any right, by virtue of the option, to participate in any share issue of the Company or any related body corporate or in the interest issue of any other registered scheme.

Environmental Regulation and Performance

There have been no known breaches by the consolidated entity of any environmental regulations or obligations.

Directors' Indemnity

During the financial year, Sunshine Heart, Inc. paid a premium of $81,121 in respect of a contract insuring all the Directors and Officers against liability, except willful breach of duty, of a nature that is required to be disclosed under section 300 (8) of the Corporations Act 2001.

The liabilities insured include costs and expenses that may be incurred in defending civil or criminal proceedings that may be brought against the officers in their capacity as officers of the Company or a related body corporate.

Remuneration Report – Audited

This Remuneration Report outlines the director and executive remuneration arrangements of the Company and the Group in accordance with the requirements of the Corporations Act 2001 and its Regulations. It also provides the remuneration disclosures required by paragraphs Aus 25.4 to Aus 25.7.2 of AASB 124 Related Party Disclosures, which have been transferred to the Remuneration Report in accordance with Corporations Regulation 2M.6.04. For the purposes of this report, Key Management Personnel of the Group are defined as those persons having authority and responsibility for planning, directing and controlling the major activities of the Company and the Group, directly or indirectly, including any director (whether executive or otherwise) of the parent Company and includes the five executives in the parent and the Group receiving the highest remuneration.

For the purposes of this report, the term 'executive' encompasses the Chief Executive, senior executives, general managers and secretaries of the parent and the Group.

Remuneration philosophy

The performance of the Company depends upon the quality of its Directors and executives. To prosper, the Company must attract, motivate and retain highly skilled Key Management Personnel. To this end, the Company embodies the following principles in its remuneration framework:

- Provide competitive rewards to attract high calibre individuals; and
- Link rewards to shareholder value.

Remuneration and nomination committee

The remuneration and nomination committee of the Board of Directors of the Company is responsible for determining and reviewing compensation arrangements for the Key Management Personnel. The committee assesses the appropriateness of the nature and amount of remuneration of the Key Management Personnel on a periodic basis by reference to relevant employment market conditions with the overall objective of ensuring maximum stakeholder benefit from the retention of a high quality team.

The remuneration and nomination committee has in place a process to review the performance of the board, sub committees and that of individual Key Management Personnel. To assist in this process an independent advisor may be used. The committee conducts a survey of directors to review the role of the board, assess the performance of the board since the previous survey and to examine ways of assisting the board in performing its duties more effectively. The issues examined include board interaction with management, the type of information provided to the board by management, and overall management performance in helping the board meet its objectives.

A similar review is performed of the board sub committees, to assist in assessing the performance of each committee and to identify areas where improvement can be made.

The committee is also responsible for reviewing the performance of Key Management Personnel. This evaluation is based on specific criteria, including the group's business performance, whether strategic objectives are being achieved and the development of management and personnel.

Further details on the remuneration of directors and executives are also provided in Note 20 to the financial statements and Table 1 and 2 of the Directors' Report.

Remuneration structure

In accordance with best practice corporate governance, the structure of non-executive director and other Key Management Personnel remuneration is separate and distinct.

Remuneration Report – Audited continued

Non-executive director remuneration

Objective

The board seeks to set aggregate remuneration at a level which provides the Company with the ability to attract and retain directors of the highest caliber, whilst incurring a cost which is acceptable to shareholders.

Structure

Remuneration consists of the following key elements:

- Fixed Remuneration; and
- Options - Long Term Incentive ('LTI') - refer below for details of the objective and structure of options granted as LTI.

The amount of fixed remuneration and share based compensation through options (potential long term incentives) is established for each non-executive director by the remuneration and nomination committee.

The ASX Listing Rules specify that the aggregate remuneration of non-executive directors shall be determined from time to time by a general meeting. An amount not exceeding the amount determined is then divided between the directors as agreed. The latest determination was at the Annual General Meeting held on 30 November 2004 when shareholders approved an aggregate remuneration of $250,000 per year. The amount of aggregate remuneration sought to be approved by shareholders and the manner in which it is apportioned amongst directors is reviewed annually. The board may consider advice from external consultants as well as the fees paid to non-executive directors of comparable companies when undertaking the annual review process.

Each non-executive director receives a fee for being a director of the Company except for Dr Geoff Brooke, Dr Richard Lin, Dr Conrad Wang and John Brennan. No additional fees are paid for each board committee on which a director sits. Non-executive directors are not required by the board to hold shares in the Company.
The remuneration of non-executive directors for the period ending 30 June 2008 is detailed in Table 1 of this report.

Key Management Personnel and Executive Director Remuneration

Objective

The Company aims to reward executives with a level and mix of remuneration commensurate with their position and responsibilities within the Company and so as to:

- align the interests of executives with those of shareholders;
- link reward with the strategic goals and performance of the Company; and
- ensure total remuneration is competitive by market standards.

Structure

In determining the level and make-up of executive remuneration, the remuneration and nomination committee primarily relies upon internal surveying of prevailing market conditions. However it may seek external advice as required.

It is the remuneration and nomination committee's policy that employment contracts are entered into with the Executive Director's and other Key Management Personnel. Details of these contracts are provided on page 16.
Remuneration consists of the following key elements:

- Fixed Remuneration – Base Salaries;
- Short Term Incentive Plan ('STIP'); and
- Long Term Incentive Plan ('LTIP').

The amount of fixed remuneration and share based compensation through options (potential long term incentives) is established for each senior manager by the remuneration and nomination committee.

Fixed Remuneration

Objective

The level of fixed remuneration is set so as to provide a base level of remuneration, which is both appropriate to the position and is competitive in the market. Fixed remuneration is reviewed annually by the remuneration and nomination committee and the process consists of a review of company wide, business unit and individual performance, relevant comparative remuneration in the market and internal and, where appropriate, external advice on policies and practices. As noted above, the committee has access to external advice independent of management.

Structure

Key Management Personnel receive their fixed (primary) remuneration in cash. The fixed remuneration component of the Key Management Personnel remuneration is detailed in Tables 1 and 2 of the Directors' Report. The Company has no other Key Management Personnel at the date of this Report.

Short Term Incentive Plan (STIP)

Objective

The objective of the STIP is to reward staff including Key Management Personnel in a manner that focuses participants on achieving personal and business goals which contribute to the creation of sustained shareholder value. Bonus differential reflects performance against these goals.

Structure

The STIP facilitates bi-annual cash and/or options bonus opportunities that reflect performance outcomes against pre-determined personal and business goals (as determined by the Board) which are key drivers for short term success and delivering long term value. The amount of any bonus is at the discretion of the Board.

Details of the cash bonuses earned under the STIP is provided in Tables 1 and 2 of the Directors' Report for Key Management Personnel and Note 15 for all employees.

Options — Long Term Incentive Plan (LTIP)

Objective

The objective of the LTIP plan is to reward staff including Key Management Personnel in a manner that aligns this element of remuneration with the creation of shareholder value. As such LTIP grants are made to staff that are able to influence the generation of shareholder wealth and thus have an impact on the Company's performance.

Structure

LTIP grants to staff including Key Management Personnel are delivered in the form of options. The Company uses a premium to the market price of the shares under option as the performance hurdle for the long-term incentive plan. Option recipients are required to meet certain length-of-service obligations.

Details of options granted, including the value of options and vesting periods under the LTIP plan, is detailed in Note 15 for employees and Note 20(c) for directors.

Remuneration Report – Audited continued

Employment and Consultancy Contracts

The Key Management Personnel salaries and fees are as set out below and are for full time services unless otherwise noted. All contracts are terminable upon one months notice, except as described below:

NAME	TITLE	ANNUAL BASE FEES
D Rohrbaugh	Chief Executive Officer	$US286,260 [1]
W Peters	Medical Director/Chief Technology Officer	$A250,140 [2]
V Windeyer	Chief Operating Officer	A$222,200 [3]
G Frugard	Vice President of Regulatory and Quality Affairs to 26 March 2008	$US207,996 [4]
B Bolton	Chief Financial Officer/Company Secretary	$A222,200 [5]
M Kepler	Director of Regulatory and Clinical Affairs from 26 March 2008	$US190,000 [6]

NOTES:

1 Mr Rohrbaugh's consulting contract commenced on 1 July 2005 and is ongoing. If Sunshine Heart terminates Mr Rohrbaugh's contract other than for cause, he is entitled to receive continued payment of his monthly fee until the earlier of: (i) the date he begins providing full time services to a third party or (ii) the six month anniversary of his termination date.

2 Dr Peters' consulting contract commenced on 3 August 2004 and is ongoing. If Sunshine Heart terminates Dr Peters' contract other than for cause, he is entitled to receive one months notice of termination, or payment in lieu of actual notice.

3 Mr Windeyer's employment contract commenced on 3 January 2006 and is ongoing. If Sunshine Heart terminates Mr Windeyer's employment other than for cause, he is entitled to receive three months notice of termination, or payment in lieu of actual notice. In addition, the Company also contributes superannuation on behalf of Mr Windeyer.

4 Mr Frugard ceased in his position as Vice President of Regulatory and Quality Affairs on 26 March 2008.

5 Mr Bolton's employment contract commenced on 16 April 2007 and is ongoing. If Sunshine Heart terminates Mr Bolton's employment other than for cause, he is entitled to receive six months notice of termination, or payment in lieu of actual notice. In addition, the Company also contributes superannuation on behalf of Mr Bolton.

6 Ms Kepler's consulting contract commenced on 15 December 2006 and is ongoing. If Sunshine Heart terminates Ms Kepler's contract other than for cause, she is entitled to receive one months notice of termination, or payment in lieu of actual notice.

Remuneration of Key Management Personnel ("KMP")

Table 1: Remuneration for the year ended **30 June 2008**

	SHORT TERM		POST EMPLOYMENT	SHARE BASED PAYMENTS	TOTAL	% PERFORMANCE RELATED [a]
	SALARY & FEES	CASH STI	SUPER-ANNUATION	OPTIONS [b]		
Non-executive Directors [c]						
M McComas	75,000	–	–	–	75,000	–
C Marsh	50,000	–	–	5,688	55,688	–
D O'Dwyer	50,000	–	–	–	50,000	–
Subtotal Non-executive Directors	175,000	–	–	5,688	180,688	
Executive Directors						
D Rohrbaugh	332,070	–	–	115,914	447,984	–
W Peters	250,140	–	–	39,196	289,336	–
Other KMP						
B Bolton	222,200	–	19,998	49,385	291,583	–
V Windeyer	222,200	–	19,998	62,588	304,786	–
G Frugard	176,605	–	–	15,579	192,184	–
M Kepler	56,568	–	–	1,543	58,111	–
Subtotal Executive KMP	1,259,783	–	39,996	284,205	1,583,984	
Total	1,434,783	–	39,996	289,893	1,764,672	

Table 2: Remuneration for the year ended **30 June 2007**

	SHORT TERM		POST EMPLOYMENT	SHARE BASED PAYMENTS	TOTAL	% PERFORMANCE RELATED [a]
	SALARY & FEES	CASH STI	SUPER-ANNUATION	OPTIONS [b]		
Non-executive Directors [c]						
M McComas	87,500	–	–	287	87,787	–
G Brooke	–	–	–	1,400	1,400	–
R Lin	–	–	–	1,522	1,522	–
C Marsh	63,219	–	–	7,429	70,648	–
D O'Dwyer	50,000	–	–	1,505	51,505	–
Sub-total Non-executive Directors	200,719	–	–	12,143	212,862	
Executive Directors						
D Rohrbaugh	364,366	51,558	–	87,504	503,428	10.25
W Peters	220,000	40,000	–	38,631	298,631	13.40
Other KMP						
B Bolton [d]	45,974	–	4,137	7,899	58,010	–
V Windeyer	163,192	62,700	20,330	87,721	333,943	20.07
A Blunden [e]	70,744	–	–	–	70,744	–
G Frugard	231,364	–	–	22,368	253,732	–
Sub-total Executive KMP	1,095,640	154,258	24,467	244,123	1,518,488	
Total	1,296,359	154,258	24,467	256,266	1,731,350	

NOTES

a No future maximum or minimum total value of performance related remuneration has been determned as at the date of this report

b Options issued to Director's related parties and other Key Management Personnel as described in Note 20(c)

c J Brennan and C Wang received no remuneration for the years ended 30 June 2008 and 30 June 2007. G Brooke and R Lin received no remuneration for the year ended 30 June 2008.

d Commenced 16 April 2007.

e Resigned as Company Secretary 16 January 2007

Remuneration Report – Audited continued

Table 3: Options granted as part of remuneration for the year ended **30 June 2008**
Nil

Table 4: Options granted as part of remuneration for the year ended **30 June 2007**

	GRANT DATE	EXERCISE PRICE $	GRANT NUMBER	VALUE PER OPTION AT GRANT DATE $	VALUE OF OPTIONS GRANTED DURING THE YEAR $	REMUNERATION CONSISTING OF OPTIONS FOR THE YEAR %
C Marsh [c]	1-Nov-06	0.30	97,000	0.0582	5,645	
C Marsh [b]	1-Nov-06	0.30	161,784	0.0582	9,415	
C Marsh [b]	18-Apr-07	0.25	50,000	0.0516	2,580	
			308,784		17,640	10.5
D Rohrbaugh [c]	1-Nov-06	0.18	640,000	0.0864	55,296	
D Rohrbaugh [a]	18 Apr-07	0.30	2,000,000	0.0878	175,600	
D Rohrbaugh [c]	18-Apr-07	0.30	3,000,000	0.0434	130,200	
			5,640,000		361,096	17.4
W Peters [c]	1-Nov-06	0.18	440,000	0.0864	38,016	
W Peters [a]	18 Apr-07	0.30	1,400,000	0.0878	122,920	
W Peters [c]	18-Apr-07	0.30	600,000	0.0434	26,040	
			2,440,000		186,976	12.9
V Windeyer [a]	31-Jan-07	0.25	1,000,000	0.1006	100,600	
V Windeyer [b]	31-Jan-07	0.25	40,000	0.1006	3,512	
V Windeyer [c]	31-Jan-07	0.30	1,000,000	0.0878	87,800	
			2,040,000		191,912	26.3
B Bolton [a]	16-Apr-07	0.25	275,000	0.0613	16,857	
B Bolton [c]	16-Apr-07	0.30	1,525,000	0.0521	79,453	
			1,800,000		96,310	13.6
G Frugard [a]	31-Jan-07	0.25	355,000	0.1006	35,713	
G Frugard [c]	31-Jan-07	0.30	280,000	0.0878	28,168	
			635,000		63,881	8.8

NOTES
a Options are performance based and will be forfeited if performance criteria is not achieved.
b Options fully vested at grant date
c Vesting is 1/4th after 1 year and 1/48th every month thereafter.

For details on the valuation of the options, including models and assumptions used, refer to Note 15. There were no alterations to the terms and conditions of options granted as remuneration since their grant date.
No options held by Key Management Personnel were exercised during the year. For details of options vested and lapsed during the year refer note 20(c).

Corporate Governance

In recognising the need for the highest standards of corporate behaviour and accountability, the Directors of Sunshine Heart, Inc. support and have adhered to the principles of corporate governance. The Company's corporate governance statement is contained in the following section of this annual report.

Auditor Independence

We have obtained the independence declaration from our auditors, Ernst & Young, a copy of which is included on page 59 of this annual report.

Directors' Meetings

The number of meetings of Directors (including meetings of committees of Directors) held during the year and the number of meetings attended by each Director were as follows:

	DIRECTORS' MEETINGS	MEETINGS OF COMMITTEES	
		AUDIT,COMPLIANCE AND GOVERNANCE	REMUNERATION AND NOMINATION
Number of meetings held:	12	4	5
Number of meetings attended:			
M McComas	12	4	–
G Brooke	11	–	5
R Lin	4	–	2
C Marsh	12	–	–
D O'Dwyer	11	4	–
W Peters	12	–	–
D Rohrbaugh *	12	–	–
J Brennan	12	–	3
C Wang	6	–	–

All directors were eligible to attend all meetings held, except for R Lin who was eligible to attend 4 Directors' meetings and C Wang who was eligible to attend 8 Directors' meetings.

Committee membership

The Company established an Audit, Compliance and Governance Committee and a Remuneration and Nomination Committee of the Board of Directors on 20 July 2004. Members acting on the committees of the board are:
Audit, Compliance and Governance - D O'Dwyer (Chairman), M McComas, C Marsh (appointed 17 July 2008)
Remuneration and Nomination - G Brooke (Chairman), R Lin (prior to resignation 15 November 2007), J Brennan (appointed 10 October 2007).

* *D Rohrbaugh is a non-voting participant at Remuneration and Nomination Committee meetings.*

Non-Audit Services

The Company's auditors, Ernst & Young, provided non-audit services during the year ended 30 June 2008.
The Directors are satisfied that the provision of non-audit services is compatible with the general standard of independence for auditors imposed by the Corporations Act. The nature and scope of each type of non-audit service provided means that auditor independence was not compromised.

Refer to Note 19 of the financial statements for details of the remuneration that Ernst & Young received or are due to receive for the provision of audit and other services.

Signed in accordance with a resolution of the Directors.

Donald Rohrbaugh
Director
Sydney, 21 August 2008

Corporate Governance Statement

Sunshine Heart's corporate governance is the system by which the Company is directed and managed. Within this framework:

- The board of directors is accountable to shareholders for the performance of the Company;
- The Company's goals to achieve milestones are set and promulgated;
- The risks of the business are identified and managed; and
- The Company's established values and principles underpin the way in which it undertakes its operations.

Sunshine Heart has in place an entrenched, highly developed governance culture which has its foundations in the ethical values that the board, management and staff bring to the Company and their commitment to positioning the Company as a world leader in heart assist technology.

This statement is organised under headings based on the Australian Securities Exchange (ASX) Corporate Governance Council's Principles of Good Corporate Governance and Best Practice Recommendations dated March 2003.

1 Lay solid foundations for management and oversight

Recognise and publish the respective roles and responsibilities of board and management

1.1 Formalise and disclose the functions reserved to the board and those delegated to management.

A copy of the Board Charter is available on the Company's website.

2 Structure the board to add value

Have a board of an effective composition, size and commitment to adequately discharge its responsibilities and duties

2.1 A majority of the board should be independent directors.

The board has a majority of non-executive directors comprising six non-executive directors and two executive directors. The ASX recommendations on director independence classify three of the non-executive directors as not independent. Dr Brooke and Mr Brennan are classified as not independent as they are associated with companies who hold a voting interest of more than 5% in Sunshine Heart. Mr Marsh who retired as an executive director of the Company in July 2006 is classified as not independent as within the last three years he was an executive of the Company. The Company's board of directors consider that Dr Brooke and Messrs Brennan and Marsh operate at all times as independent directors and in the best interest of all shareholders. The Company considers the following six directors to be independent: Messrs McComas (Chairman), Brennan, Callinan, Marsh and O'Dwyer and Dr Brooke.

The Company considers that the composition of the board is appropriate as Dr Brooke and Mr Brenan are experienced venture capital managers who bring to the board particular expertise in the management and development of early stage medical device companies and Mr Marsh, a co-founder of the Company, offers substantial strategic foresight in commercialising the Company's technology.

2.2 The chairman should be an independent director.

The Board Charter requires the chairman to be independent.

2.3 The roles of chairman and chief executive officer should not be exercised by the same individual.

The Board Charter requires the chairman and the chief executive officer to be different individuals.

2.4 The Board should establish a nomination committee.

The Company has a Remuneration and Nomination Committee comprising two non-executive directors. The combined role is considered appropriate for a company of this size. A copy of the Remuneration and Nomination Committee Charter is available on the Company's website.

2.5 *Independent professional advice*

The Board has an agreed procedure for directors and board committees to obtain independent professional advice at the Company's expense.

3 Promote ethical and responsible decision making

Actively promote ethical and responsible decision making

3.1 *Establish a code of conduct to guide the directors, the chief executive officer (or equivalent), the chief financial officer (or equivalent) and any other key executives as to:*

- ***the practices necessary to maintain confidence in the company's integrity;***
- ***the responsibility and accountability of individuals for reporting and investigating reports of unethical practices.***

A copy of the Code of Conduct is available on the Company's website.

3.2 *Disclose the policy concerning trading in company securities by directors, officers and employees.*

A copy of the Company's Share Trading Policy is available on the Company's website.

4 Safeguard integrity in financial reporting

Have a structure to independently verify and safeguard the integrity of the company's financial reporting

4.1 *Require the chief executive officer and the chief financial officer to state in writing to the board that the company's financial reports present a true and fair view, in all material respects, of the company's financial condition and operational results and are in accordance with relevant accounting standards.*

The Company's board requires a statement in writing from the chief executive officer and chief financial officer attesting to requirements in recommendation 4.1.

4.2 *The board should establish an audit committee.*

The Company has an Audit, Compliance and Corporate Governance ("Audit") Committee.

4.3 *Structure the audit committee so that it consists of:*

- ***only non-executive directors***
- ***majority of independent directors***
- ***an independent chairman, who is not chairman of the board***
- ***at least three members.***

The Audit Committee has three non-executive members, a majority of independent directors and its chairman is not chairman of the board. The size of the Audit Committee is appropriate to the size of the Company.

4.4 *The audit committee should have a formal charter.*

The Audit Committee Charter is available on the Company's website.

5 Make timely and balanced disclosure

Make timely and balanced disclosure of all material matters concerning the company

5.1 *Establish written policies and procedures designed to ensure compliance with ASX Listing Rule disclosure requirements and to ensure accountability at a senior management level for that compliance.*

The Company has a Continuous Disclosure and Shareholder Communication Policy to ensure compliance with ASX Listing Rule disclosure requirements and to ensure accountability at a senior management level for that compliance. A copy of the Policy is available on the Company's website.

6 Respect the rights of shareholders

Respect the rights of shareholders and facilitate the effective exercise of those rights

6.1 Design and disclose a communications strategy to promote effective communication with shareholders and encourage effective participation at general meetings.

Sunshine Heart provides shareholders with quarterly updates of the Company's progress across all areas of the business (in addition to continuous disclosure requirements), and utilises its website to disclose useful and relevant information about the Company. The Company's Continuous Disclosure and Shareholder Communication Policy is available on its website.

6.2 Request the external auditor to attend the annual general meeting and be available to answer shareholder questions about the conduct of the audit and the preparation and content of the auditor's report.

The Company's Continuous Disclosure and Shareholder Communication Policy requires that the external auditor be requested to attend annual general meetings and be able to answer shareholder questions.

7 Recognise and manage risk

Establish a sound system of risk oversight and management and internal control

7.1 The board or appropriate board committee should establish policies on risk oversight and management.

The Audit Committee is responsible to the Board for oversight in this area. The Company's Risk Management Statement which provides an overview of the Company's risk profile and management strategies is available on its website.

7.2 The chief executive officer (or equivalent) and the chief financial officer (or equivalent) should state to the board in writing that:

(i) the statement given in 4.1 above is founded on a sound system of risk management and internal compliance and control that implements policies adopted by the board; and

(ii) the company's risk management and internal compliance and control system is operating effectively in all material respects.

The board requires a statement in writing from the chief executive officer and chief financial officer attesting to the above requirements.

8 Encourage enhanced performance

Fairly review and actively encourage enhanced board and management effectiveness

8.1 Disclose the process for performance evaluation of the board, its committees and individual directors, and key executives.

The Board undertakes an annual process of assessing both the performance of the board and its committees, as well as the individual performance of directors and key executives. To ensure this process is objective and constructive, external advisors may assist the board and provide independent advice to enhance and improve the process and the board's performance. During the year the performance of the board and each committee were assessed as well as the individual performance of directors and key executives. Areas for improvement were identified and strategies adopted to implement improvements.

9 Remunerate fairly and responsibly

Ensure that the level and composition of remuneration is sufficient and reasonable and that its relationship to corporate and individual performance is defined

9.1 Provide disclosure in relation to the company's remuneration policies to enable investors to understand:

(i) the costs and benefits of those policies; and

(ii) the link between remuneration paid to directors and key executives and corporate performance

The Company's Annual Report includes a remuneration report that discloses the principles used to determine the nature and amount of remuneration, details of remuneration including incentive payments, service agreements, share-based compensation and loans to directors and senior executives. The Company's Annual Report is available on its website.

9.2 The board should establish a remuneration committee.

The Company has a Remuneration and Nomination Committee. A copy of the Remuneration and Nomination Committee Charter is available on the Company's website.

9.3 Clearly distinguish the structure of non-executive Directors' remuneration from that of executives.

The Company's policy is to reward executives with a combination of fixed remuneration and short and long term incentives, structured to drive improvements in shareholder value. Non-executive directors receive no incentive cash payments other than their fixed fee. Non-executive directors have received shareholder approved share options which are normally issued at premium to the then share price. Any benefit to directors will only accrue from an increase in share price.

9.4 Ensure that payment of equity-based executive remuneration is made in accordance with thresholds set in plans approved by shareholders.

The Company's Stock Option Plan (SOP) was approved by shareholders in May 2003. Future amendments to the SOP, the introduction of any other equity-based remuneration schemes, or the issue of further options to directors will be approved by shareholders as required before being implemented.

10 Recognise the legitimate interests of stakeholders

Recognise legal and other obligations to all legitimate stakeholders

10.1 Establish and disclose a code of conduct to guide compliance with legal and other obligations to legitimate stakeholders.

A copy of the Code of Conduct is available on the Company's website.

Income Statement

For the year ended 30 June 2008

	NOTES	CONSOLIDATED		SUNSHINE HEART, INC.	
		2008	2007	2008	2007
		$	$	$	$
Revenue and other income	3	**441,121**	3,220,722	**360,914**	485,291
Write-down of investments	3	**–**	–	**(9,357,218)**	(11,243,813)
Depreciation and amortisation	3	**(78,277)**	(64,269)	**–**	–
Insurance		**(110,945)**	(174,878)	**(77,874)**	(106,698)
Listing fees		**(36,112)**	(19,241)	**(36,112)**	(19,241)
Office expenses	3	**(177,259)**	(155,817)	**–**	(3,588)
Professional fees		**(233,280)**	(338,394)	**(166,464)**	(289,180)
Salaries and employee benefits	3	**(2,159,742)**	(2,371,082)	**–**	–
Research and development	3	**(5,834,795)**	(10,295,675)	**–**	–
Travel		**(529,479)**	(554,056)	**(8,257)**	(12,899)
Patents		**(151,364)**	(80,947)	**–**	–
Other expenses		**(868,051)**	(705,776)	**(453,172)**	(349,285)
Loss before income tax		**(9,738,183)**	(11,539,413)	**(9,738,183)**	(11,539,413)
Income tax benefit	4	**–**	–	**–**	–
Loss after income tax		**(9,738,183)**	(11,539,413)	**(9,738,183)**	(11,539,413)
Loss for the year attributable to members of Sunshine Heart, Inc.	12(e)	**(9,738,183)**	(11,539,413)	**(9,738,183)**	(11,539,413)
Basic loss per share (cents per share)	18	**(4.8)**	(8.3)		
Diluted loss per share (cents per share)	18	**(4.8)**	(8.3)		

Balance Sheet

At 30 June 2008

	NOTES	CONSOLIDATED 2008 $	CONSOLIDATED 2007 $	SUNSHINE HEART, INC. 2008 $	SUNSHINE HEART, INC. 2007 $
ASSETS					
Current Assets					
Cash and cash equivalents	13(b)	**9,772,617**	7,718,498	**8,998,841**	5,248,426
Other current assets	5	**94,071**	120,725	**–**	22,654
Other receivables	6	**59,056**	183,385	**59,056**	26,536
Total Current Assets		**9,925,744**	8,022,608	**9,057,897**	5,297,616
Non-Current Assets					
Property, plant and equipment	9	**252,710**	358,899	**–**	–
Other financial assets	7	**–**	–	**878,697**	2,906,086
Total Non-Current Assets		**252,710**	358,899	**878,697**	2,906,086
Total Assets		**10,178,454**	8,381,507	**9,936,594**	8,203,702
LIABILITIES					
Current Liabilities					
Trade and other payables	10	**152,447**	189,242	**1,692**	79,954
Provisions	11	**91,105**	68,517	**–**	–
Total Current Liabilities		**243,552**	257,759	**1,692**	79,954
Total Liabilities		**243,552**	257,759	**1,692**	79,954
Net Assets		**9,934,902**	8,123,748	**9,934,902**	8,123,748
EQUITY					
Contributed equity	12(a)	**48,293,638**	37,074,128	**48,293,638**	37,074,128
Accumulated losses	12(e)	**(39,953,391)**	(30,215,208)	**(39,953,391)**	(30,215,208)
Reserves	12(f)	**1,594,655**	1,264,828	**1,594,655**	1,264,828
Total Equity		**9,934,902**	8,123,748	**9,934,902**	8,123,748

Statement of Recognised Income and Expense

For the year ended 30 June 2008

	CONSOLIDATED		SUNSHINE HEART, INC.	
	2008	2007	2008	2007
	$	$	$	$
Net income recognised directly in equity	**–**	–	**–**	–
Loss for the year	**(9,738,183)**	(11,539,413)	**(9,738,183)**	(11,539,413)
Total recognised income and expense for the year	**(9,738,183)**	(11,539,413)	**(9,738,183)**	(11,539,413)
Attributable to:				
Equity holders of Sunshine Heart, Inc.	**(9,738,183)**	(11,539,413)	**(9,738,183)**	(11,539,413)

Cash Flow Statement

For the year ended 30 June 2008

	NOTES	CONSOLIDATED 2008 $	CONSOLIDATED 2007 $	SUNSHINE HEART, INC. 2008 $	SUNSHINE HEART, INC. 2007 $
Cash flows from operating activities					
Receipt of government grants		**143,045**	2,633,024	**–**	–
Payments to suppliers and employees		**(9,717,518)**	(13,157,861)	**(806,855)**	(705,854)
Interest received		**422,611**	527,345	**342,404**	486,139
Net cash flow used in operating activities	13(a)	**(9,151,862)**	(9,997,492)	**(464,451)**	(219,715)
Cash flows from investing activities					
Investment in subsidiary		**–**	–	**(7,000,000)**	(11,750,000)
Purchase of property, plant and equipment		**(8,885)**	(174,246)	**–**	–
Net cash flows used in investing activities		**(8,885)**	(174,246)	**(7,000,000)**	(11,750,000)
Cash flows from financing activities					
Proceeds from issue of ordinary shares		**11,445,542**	13,802,396	**11,445,542**	13,802,396
Proceeds from repayment of loan by subsidiary		**–**	–	**–**	307,735
Payment of share issue costs		**(226,032)**	(366,726)	**(226,032)**	(366,726)
Net cash flows from financing activities		**11,219,510**	13,435,670	**11,219,510**	13,743,405
Net increase in cash and cash equivalents		**2,058,763**	3,263,932	**3,755,059**	1,773,690
Net foreign exchange differences		**(4,644)**	(77,408)	**(4,644)**	(77,408)
Cash and cash equivalents at beginning of year		**7,718,498**	4,531,974	**5,248,426**	3,552,144
Cash and cash equivalents at end of year	13(b)	**9,772,617**	7,718,498	**8,998,841**	5,248,426

Notes to the Financial Statements

For the year ended 30 June 2008

1. Corporate Information

The annual report of Sunshine Heart, Inc. ("Company" or "Sunshine Heart") for the year ended 30 June 2008 was authorised for issue in accordance with a resolution of the directors on 21 August 2008.

Sunshine Heart, Inc. ("Company" or "Sunshine Heart") is a company limited by shares incorporated in Delaware, United States of America. Its shares are publicly traded on the Australian stock exchange, ASX code: SHC.

The nature of the operations and principal activities of the Group are to design and develop a heart assist device.

2. Summary of Significant Accounting Policies

(a) Basis of Preparation

Sunshine Heart is a foreign company registered under Part 5B.2 of the Corporations Act 2001. The financial report is a general purpose financial report and has been prepared to satisfy the requirements of the Corporations Act 2001 and Australian Accounting Standards. The financial report is presented in Australian dollars and has been prepared on a historical cost basis.

(b) Statement of compliance

The financial report complies with Australian Accounting Standards. The financial report also complies with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board.

Certain Australian Accounting Standards and UIG interpretations have been recently issued or amended but are not yet effective. These other standards have not been adopted by the Group for the year ended 30 June 2008. The Directors have yet to finalise their assessment of the impact of these new or amended standards (to the extent relevant to the Group) and interpretations.

Adoption of new accounting standard

The Group has adopted AASB 7 Financial Instruments; Disclosures and all consequential amendments. The adoption of this standard has only affected the disclosure in these financial statements. There has been no affect on profit and loss or the financial position of the Company or Group.

(c) Going Concern

The Group's financial statements have been prepared and presented on a basis assuming it continues as a going concern.

During the years ended 30 June 2008 and 30 June 2007, the Group incurred an operating loss before tax and net cash outflows from operating activities as disclosed in the income statement and cash flow statement, respectively.

The Group's ability to continue as a going concern is dependent on the Group's ability to raise additional capital based on the achievement of its existing milestones as and when required. The directors, after due consideration, believe that the Group will be able to raise new equity capital as required to fund its business plan. Should the future capital raising not be successful, the Group may not be able to continue as a going concern. Furthermore, the ability of the Group to continue as a going concern is subject to the ability of the Group to develop and successfully commercialise the product being developed. If the Group is unable to obtain such funding of an amount and timing necessary to meet its future operational plans, or to successfully commercialise its intellectual property, the Group may be unable to continue as a going concern. No adjustments have been made relating to the recoverability and classification of recorded asset amounts and classification of liabilities that might be necessary should the Group not continue as a going concern.

For the year ended 30 June 2008

2. Summary of Significant Accounting Policies continued

(d) Basis of consolidation

The consolidated financial statements comprise the financial statements of Sunshine Heart, Inc. and its subsidiary as at 30 June each year (the Group). The financial statements of the subsidiary are prepared for the same reporting period as the parent Company, using consistent accounting policies. In preparing the consolidated financial statements, all intercompany balances and transactions, income and expenses and profit and losses resulting from intra-group transactions have been eliminated in full. Subsidiaries are fully consolidated from the date on which control is transferred to the Group and cease to be consolidated from the date on which control is transferred out of the Group

(e) Significant accounting estimates and assumptions

The carrying amounts of certain assets and liabilities are often determined based on estimates and assumptions of future events. The key estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of certain assets and liabilities within the next annual reporting period are:

Share-based payment transactions

The consolidated Group provides benefits to employees, consultants and directors in the form of share-based payment transactions, whereby employees render services in exchange for share options ('equity-settled transactions') under the 2002 Stock Plan ('the Plan'). The Group measures the cost of equity-settled transactions by reference to the fair value of the equity instruments at the date at which they are granted. The fair value is determined by using the Black-Scholes formula taking into account the terms and conditions upon which the instruments were granted, as discussed in Note 15.

Impairment of investment in subsidiary

The Group assesses impairment of its investment in its subsidiary at each reporting date by evaluating conditions specific to the Group and to the subsidiary that may lead to impairment. This includes product performance, technology, economic and political environment and future product expectations. If an impairment trigger exists the recoverable amount of the asset is determined. The assumptions used in determining the recoverable amount are discussed in Note 8.

(f) Revenue recognition

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised:

(i) Grant income

Grants from the government are recognised at their fair value where there is reasonable assurance that the grant will be received and the Group will comply with all attached conditions.

Where the grant relates to an expense item, it is recognised as income over the periods necessary to match the grant on a systematic basis to the costs it intends to compensate. When the grant relates to an asset, the fair value is credited to a deferred income account and is released to the income statement over the expected useful life of the relevant asset by equal annual instalments. Where government payments are received in advance of expenditure, a present obligation exists to repay the government under the conditions of the grant. This is recognised as deferred income. Where government grants are received in arrears of expenditure, a future economic benefit exists with funds owed by the government under the conditions of the grant. This is recognised within other receivable, refer Note 6.

(ii) Interest income

Interest revenue is recognised as it accrues, taking into account the effective yield on the financial asset.

(g) Borrowing costs

Borrowing costs are recognised as an expense when incurred. The Group does not currently hold qualifying assets but, if it did, the borrowing costs directly associated with this asset would be capitalised (including any other associated costs directly attributable to the borrowing and temporary investment income earned on the borrowing).

(h) Leases

The determination of whether an arrangement is or contains a lease is based on the substance of the arrangement and requires an assessment of whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets and the arrangement conveys a right to use the asset.

Group as a lessee

Operating lease payments are recognised as an expense in the income statement on a straight-line basis over the lease term. Lease incentives are recognised in the income statement as an integral part of the total lease expense.

(i) Cash and cash equivalents

Cash and short term deposits in the balance sheet comprise cash at bank and in hand and short term deposits with an original maturity of three months or less. For the purposes of the cash flow statement, cash and cash equivalents consist of cash and cash equivalents as defined above, net of outstanding bank overdrafts.

(j) Other receivables

Other receivables generally have 30-90 day terms and are recognised and carried at nominal contractual amounts less an allowance for any uncollectible amounts. The doubtful debts allowance is made when objective evidence suggests the Group will be unable to collect the debts and bad debts are written off when identified.

For the year ended 30 June 2008

2. Summary of Significant Accounting Policies continued

(k) Foreign currency translation

Both the functional and presentation currency of Sunshine Heart, Inc. and it Australian subsidiary is Australian dollars (A$). Each entity in the Group determines its own functional currency and items included in the financial statements of each entity are measured using that functional currency.

Transactions in foreign currencies are initially recorded in the functional currency at the exchange rates ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the rate of exchange ruling at the balance sheet date. All exchange differences in the consolidated report are taken to the income statement. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate as at the date of the initial transaction.

(l) Income tax

Current tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted by the balance sheet date.

Deferred income tax liabilities are recognised for all taxable differences except when the taxable temporary difference is associated with an investment in a subsidiary and the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred income tax assets are recognised for all deductible temporary differences, carry-forward of unused tax assets and unused tax losses to the extent that it is probable that taxable profit will be available against which the deductible temporary differences and the carry-forward of unused tax credits and unused tax losses can be utilised except when the deferred income tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

The carrying amount of deferred income tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilised.

Unrecognised deferred income tax assets are reassessed at each balance sheet date and are recognised to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the balance sheet date.

Income taxes relating to items recognised directly in equity are recognised in equity and not in the income statement.

Deferred tax assets and deferred tax liabilities are offset only if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred tax assets and liabilities relate to the same taxable entity and the same taxation authority

(m) Other taxes

Revenues, expenses and assets are recognised net of the amount of GST except:

- when the GST on a purchase of goods and services is not recoverable from the taxation authority, in which case the GST is recognised as part of the cost of acquisition of the asset or as part of the expense item as applicable; and
- receivables and payables, which are stated with the amount of GST included.

The net amount of GST recoverable from, or payable to, the taxation authority is included as part of receivables or payables in the balance sheet.

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

Commitments and contingencies are disclosed net of the amount of GST recoverable from, or payable to, the taxation authority.

(n) Property, plant and equipment

Plant and equipment is stated at cost less accumulated depreciation and any impairment in value. Depreciation is calculated on a straight line basis over the estimated useful life of the asset. The depreciation rates used for each class of asset are as follows (applicable for 2008/2007):

Office furniture and equipment	10 - 15 years
Computer equipment	3 - 4 years
Laboratory and research equipment	3 - 15 years.

Leasehold improvements are stated at cost less accumulated amortisation and any impairment in value. Amortisation is calculated on a straight line basis over the shorter of the estimated useful life of the asset or the lease term.

(i) Impairment

The carrying values of plant and equipment are reviewed for impairment when events or changes in circumstances indicate the carrying value may not be recoverable. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash generating unit to which the asset belongs. If any such indication exists and where the carrying values exceed the estimated recoverable amount, the assets or cash generating units are written down to their recoverable amount.

The recoverable amount of plant and equipment is the greater of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and risks specific to the asset.

(ii) Derecognition and disposal

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset.

For the year ended 30 June 2008

2. Summary of Significant Accounting Policies continued

(o) Other financial assets

Investment in a controlled entity is carried at the lower of cost or recoverable amount and reviewed at each balance date to reflect the Company's interest in the underlying net asset value of the controlled entity.

Impairment

The carrying value is reviewed for impairment when events or changes in circumstances indicate the carrying value may not be recoverable. If any such indication exists and where the carrying values exceed the estimated recoverable amount, the assets or cash generating units are written down to their recoverable amount. The amount of the loss is recognised in the Income Statement

(p) Intangible assets

Intangible assets acquired separately or in a business combination are initially measured at cost. The cost of an intangible asset acquired in a business combination is its fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. Internally generated intangible assets, excluding capitalised development costs, are not capitalised and expenditure is charged to the income statement in the year in which the expenditure is incurred. The amortisation period and method are reviewed annually, to ensure that they reflect the expected pattern of consumption of embodied, future economic benefits.

(i) Research and development expenditure

The consolidated Group expenses all research expenditure as incurred including expenditure made on the C-Pulse and other related technologies. Development expenditure is carried forward when its future recoverability can be regarded as assured.

(ii) Patents and trademarks

All patent, licence and trademarks expenditure is expensed as incurred as the Group has not yet developed a commercial product.

The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortised over the useful life and tested for impairment whenever there is an indication that the intangible asset may be impaired. The amortisation period and the amortisation method for an intangible asset with a finite useful life is reviewed at least each financial year-end. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset are accounted for prospectively by changing the amortisation period or method, as appropriate which is a change in accounting estimate. The amortisation expense on intangible assets with finite lives is recognised in profit or loss in the expense category consistent with the function of the intangible asset.

Intangible assets with indefinite useful lives are tested for impairment annually either individually or at the cash generating unit level. Such intangibles are not amortised. The useful life of an intangible asset with an indefinite life is reviewed each reporting period to determine whether indefinite life assessment continues to be supportable. If not, the change in the useful life assessment from indefinite to finite is accounted for as a change in an accounting estimate and is thus accounted for on a prospective basis.

(q) Trade and other payables

Trade payables and other payables are carried at amortised costs and represent liabilities for goods and services provided to the Group prior to the end of the financial year that are unpaid and arise when the Group becomes obliged to make future payments in respect of the purchase of these goods and services.

(r) Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

When the Group expects some or all of a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain. The expense relating to any provision is presented in the income statement net of any reimbursement.

If the effect of the time value of money is material, provisions are discounted using a current pre-tax rate that reflects the risks specific to the liability. When discounting is used, the increase in the provision due to the passage of time is recognised as a borrowing cost.

(s) Employee leave benefits

(i) Wages, salaries, annual leave and sick leave

Liabilities for wages and salaries, including non-monetary benefits and annual leave expected to be settled within 12 months of the reporting date are recognised in provisions in respect of employees' services up to the reporting date. They are measured at the amounts expected to be paid when the liabilities are settled.

(ii) Long service leave

The liability for long service leave is recognised in the provision for employee benefits and measured as the present value of expected future payments to be made in respect of services provided by employees up to the reporting. Consideration is given to expected future wage and salary levels, experience of employee departures, and periods of service. Expected future payments are discounted using market yields at the reporting date on national government bonds with terms to maturity and currencies that match, as closely as possible, the estimated future cash outflows.

(t) Pensions and other post employment benefits

All Australian employees are entitled to varying levels of benefits on retirement, disability or death. The superannuation plans provide accumulated benefits. Employees contribute to the plans at various percentages of their wages and salaries. Contributions by the consolidated entity of up to 9% of employees' wages and salaries are legally enforceable in Australia.

For the year ended 30 June 2008

2. Summary of Significant Accounting Policies continued

(u) Share-based payment transactions

Equity settled transactions

The Group provides benefits to employees (including Directors) in the form of share-based payments, whereby employees render services in exchange for options over shares (equity settled transactions) under Sunshine Heart's 2002 Stock Plan ("the Plan").

The cost of these equity-settled transactions with employees is measured by reference to the fair value of the equity instruments at the date at which they are granted. The fair value is determined using a Black-Scholes model, details of which are given in Note 15. In valuing equity-settled transactions, no account is taken of any performance conditions, other than conditions linked to the price of the shares of Sunshine Heart (market conditions).

The cost of equity-settled transactions is recognised, together with a corresponding increase in equity, over the period in which the performance and/or service conditions are fulfilled, ending on the date on which the relevant employees become entitled to the award (the vesting period).

The cumulative expense recognised for equity-settled transactions at each reporting date until vesting date reflects (i) the extent to which the vesting period has expired and (ii) the Group's best estimate of the number of equity instruments that will ultimately vest. No adjustment is made for the likelihood of market performance conditions being met as the effect of these conditions is included in the determination of fair value at grant date. The income statement charge or credit for a period represents the movement in cumulative expense recognised as at the beginning and end of that period.

No expense is recognised for awards that do not ultimately vest, except for awards where vesting is only conditional upon a market condition.

If the terms of an equity-settled award are modified, as a minimum an expense is recognised as if the terms had not been modified. In addition, an expense is recognised for any modification that increases the total fair value of the share based payment arrangement, or is otherwise beneficial to the employee, as measured at the date of modification.

If an equity-settled award is cancelled, it is treated as if it had vested on the date of cancellation, and any expense not yet recognised for the award is recognised immediately. However, if a new award is substituted for the cancelled award and designated as a replacement award on the date that it is granted, the cancelled and new award are treated as if they were a modification of the original award, as described in the previous paragraph.

The dilutive effect, if any of options is reflected as additional share dilution in the computation of earnings per share.

(v) Contributed equity

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new equity instruments are shown in equity as a deduction, net of tax, from the proceeds.

(w) Warrants

Warrants are classified as equity as the number of ordinary shares that will be issued upon their exercise is fixed. The fair value was determined using the Black-Scholes model.

(x) Earnings Per Share

Basic EPS is calculated as a net loss attributable to members, adjusted to exclude costs of servicing equity (other than dividends), divided by the weighted average number of ordinary shares.

Diluted EPS is calculated as net loss attributable to members, adjusted for:

- Costs of servicing equity (other than dividends)
- The after-tax effect of dividends and interest associated with dilutive potential ordinary shares that have been recognised as expenses; and
- Other non-discretionary changes in revenues or expenses during the period that would result from the dilution of potential ordinary shares;

divided by the weighted average number of ordinary shares and dilutive potential ordinary shares.

At present the potential ordinary shares are anti-dilutive and have not been included in the dilutive earnings per share calculation.

	NOTES	CONSOLIDATED		SUNSHINE HEART, INC.	
		2008	2007	2008	2007
		$	$	$	$
3. Revenues and Expenses					
(a) Revenue and other Income					
Government grants		**–**	2,694,224	**–**	–
Finance revenue – bank interest		**441,121**	526,498	**360,914**	485,291
		441,121	3,220,722	**360,914**	485,291
(b) Write-down of investments in subsidiary		**–**	–	**9,357,218**	11,243,813
(c) Depreciation and amortisation					
Depreciation – plant and equipment		**63,289**	55,747	**–**	–
Amortisation – leasehold improvements		**14,988**	8,522	**–**	–
		78,277	64,269	**–**	–
(d) Operating lease rental					
Lease payments		**177,259**	155,817	**–**	3,588
(e) Employee benefits expense					
Share based payments	12(f)	**329,827**	319,760	**–**	–
Employee benefits		**75,978**	27,908	**–**	–
Superannuation		**116,840**	97,820	**–**	–
Salaries		**1,637,097**	1,925,594	**–**	–
		2,159,742	2,371,082	**–**	–
(f) Research and development expenses		**5,834,795**	10,295,675	**–**	–
(g) Foreign exchange differences					
Net foreign exchange (gain)/loss		**(4,644)**	(20,875)	**(4,644)**	(20,875)

For the year ended 30 June 2008

	CONSOLIDATED		SUNSHINE HEART, INC.	
	2008	2007	2008	2007
	$	$	$	$
4. Income Tax				
A reconciliation between tax expense and the product of accounting loss before income tax multiplied by the Group's applicable income tax rate is as follows:				
Accounting loss before tax from continuing operations	**(9,738,183)**	(11,539,413)	(9,738,183)	(11,539,413)
At the Group statutory income tax rate of 39% (2007: 39%)	**(3,797,891)**	(4,500,371)	(3,797,891)	(4,500,371)
Expenditure not allowed for income tax purposes				
– share based payments	**128,633**	124,706	–	–
– write-down of investment in subsidiary	**–**	–	3,649,315	4,385,088
Difference in overseas tax rates	**35,531**	974,837	–	–
Other	**303,967**	40,134	(1,183)	96,378
Current year tax losses not booked as a future tax benefit, as a realisation of benefit is not probable	**3,329,760**	3,360,694	149,760	18,905
Income tax benefit reported in the consolidated income statement	**–**	–	–	–
Income Tax Losses				
Future deferred tax asset arising from tax losses not recognised at reporting date as realisation of the benefit is not regarded as probable	**10,475,152**	7,601,576	612,899	650,188

The unrecognised deferred tax assets relating to deductible temporary differences at 30 June 2008 is $87,674 (2007: $46,558). The unrecognised deferred tax liabilities relating to assessable temporary differences at 30 June 2008 is nil (2007: nil). The aggregate temporary differences associated with the investment in Sunshine Heart Company Pty Limited are nil (2007: nil).

Consolidated franking account balance at 30 June 2008 nil (2007: nil).

	CONSOLIDATED		SUNSHINE HEART, INC.	
	2008	2007	2008	2007
	$	$	$	$

5. Other Current Assets

Prepayments and deposits	**94,071**	120,725	**–**	22,654

6. Other Receivables (current)

Other receivables	**26,256**	26,051	**26,256**	12,246
Finance revenue receivables–bank interest	**32,800**	14,290	**32,800**	14,290
Government grant (Note 16)	**–**	143,044	**–**	–
	59,056	183,385	**59,056**	26,536

Other receivables are non-interest bearing and generally on 30-90 day terms.

Financial revenue receivable relates to a 30 day term deposit.

No receivables are impaired.

7. Other Financial Assets (non-current)

Investments at cost comprise:				
Investment in controlled entity	**–**	–	**34,763,244**	27,763,244
Share based payments – options issued *	**–**	–	**1,594,655**	1,264,828
Less provision for write-down in investment	**–**	–	**(35,479,202)**	(26,121,986)
Total investments (Note 8)	**–**	–	**878,697**	2,906,086

* Share options issued to employees in Sunshine Heart Company Pty Limited. Refer to Note 12.

8. Interests in Subsidiaries

NAME	COUNTRY OF INCORPORATION	EQUITY INTEREST HELD BY THE CONSOLIDATED ENTITY	INVESTMENT	
		2008/2007	2008	2007
		%	$	$
Sunshine Heart Company Pty Limited	Australia	100	**878,697**	2,906,086

During the year ended 30 June 2008, Sunshine Heart, Inc. subscribed for an additional 7,000,000 ordinary fully paid shares in Sunshine Heart Company Pty Limited. The cost of acquisition was $7,000,000. Furthermore, Sunshine Heart, Inc. made additional non-cash investments into its wholly owned subsidiary during the year in recognition of the share based payments expense (options remuneration) that was charged to the subsidiary's income statement for $329,827 and accumulated amount for prior years for $1,264,828. The carrying value of this investment has been written down to its recoverable amount, as regulatory approval has not yet been obtained. The Directors have determined the recoverable amount to be the fair value by reference to the stage of development of the Company being the net asset position of the subsidiary at balance date.

For the year ended 30 June 2008

	NOTES	CONSOLIDATED 2008 $	CONSOLIDATED 2007 $	SUNSHINE HEART, INC. 2008 $	SUNSHINE HEART, INC. 2007 $
9. Property, Plant and Equipment					
Leasehold Improvements					
At cost		**77,241**	77,241	–	–
Accumulated amortisation		**(25,086)**	(10,098)	–	–
	9(a)	**52,155**	67,143	–	–
Office Furniture and Equipment					
At cost		**88,443**	87,942	–	–
Accumulated depreciation		**(15,849)**	(9,357)	–	–
	9(a)	**72,594**	78,585	–	–
Computer Equipment					
At cost		**56,523**	126,450	–	–
Accumulated depreciation		**(17,713)**	(65,702)	–	–
	9(a)	**38,810**	60,748	–	–
Laboratory and Research Equipment					
At cost		**177,083**	288,757	–	–
Accumulated depreciation		**(87,932)**	(136,334)	–	–
	9(a)	**89,151**	152,423	–	–
Total Property, Plant and Equipment					
At cost		**399,290**	580,390	–	–
Accumulated depreciation and amortisation		**(146,580)**	(221,491)	–	–
Total written down amount		**252,710**	358,899	–	–

9. Property, Plant and Equipment continued

(a) Reconciliations

Reconciliations of the carrying amounts of property, plant and equipment at the beginning and end of the current financial year.

	2008 $	2007 $
Leasehold Improvements		
Carrying amount at beginning	**67,143**	32,100
Additions	**–**	43,565
Amortisation expense	**(14,988)**	(8,522)
Net Carrying Amount	**52,155**	67,143
Office Furniture and Equipment		
Carrying amount at beginning	**78,585**	55,762
Additions	**500**	28,395
Depreciation expense	**(6,491)**	(5,572)
Net Carrying Amount	**72,594**	78,585
Computer Equipment		
Carrying amount at beginning	**60,748**	45,629
Additions	**8,385**	33,175
Depreciation expense	**(20,499)**	(18,056)
Disposals	**(9,824)**	–
Net Carrying Amount	**38,810**	60,748
Laboratory and Research Equipment		
Carrying amount at beginning	**152,423**	115,430
Additions	**–**	69,112
Depreciation expense	**(36,299)**	(32,119)
Disposals	**(26,973)**	–
Net Carrying Amount	**89,151**	152,423
Total Property, Plant and Equipment		
Carrying amount at beginning	**358,899**	248,921
Additions	**8,885**	174,247
Depreciation expense	**(78,277)**	(64,269)
Disposals	**(36,797)**	–
Net Carrying Amount	**252,710**	358,899

No property, plant and equipment is impaired.

For the year ended 30 June 2008

	CONSOLIDATED		SUNSHINE HEART, INC.	
	2008	2007	2008	2007
	$	$	$	$
10. Trade and Other Payables (current)				
Sundry creditors	**152,447**	189,242	**1,692**	79,954
	152,447	189,242	**1,692**	79,954

Sundry creditors are non-interest bearing and are normally settled on 30 day terms.

11. Provisions (current)

	CONSOLIDATED 2008 $	CONSOLIDATED 2007 $	SUNSHINE HEART, INC. 2008 $	SUNSHINE HEART, INC. 2007 $
Annual leave	**84,705**	66,517	**–**	–
Long service leave	**6,400**	2,000	**–**	–
	91,105	68,517	**–**	–
Movement in annual leave provision				
Balance 1 July 2007	**66,517**	40,608	**–**	–
Arising during the year	**95,784**	85,041	**–**	–
Utilised	**(77,596)**	(59,132)	**–**	–
Balance at 30 June 2008	**84,705**	66,517	**–**	–
Movement in long service leave provision				
Balance 1 July 2007	**2,000**	–	**–**	–
Arising during the year	**4,400**	2,000	**–**	–
Balance at 30 June 2008	**6,400**	2,000	**–**	–

12. Contributed Equity and Reserves

	CONSOLIDATED 2008 $	CONSOLIDATED 2007 $	SUNSHINE HEART, INC. 2008 $	SUNSHINE HEART, INC. 2007 $
(a) Issued and paid up capital				
Shares, fully paid	**46,914,438**	35,694,928	**46,914,438**	35,694,928
Warrants	**1,379,200**	1,379,200	**1,379,200**	1,379,200
	48,293,638	37,074,128	**48,293,638**	37,074,128

	2008 NUMBER OF SHARES	2008 $	2007 NUMBER OF SHARES	2007 $
(b) Movement in shares on issue				
Shares, fully paid				
Beginning of the financial year	173,930,969	35,694,928	81,917,328	22,259,263
Issued on 15 November 2006 for cash as first tranche of placement	–	–	92,013,641	13,802,391
Issued on 1 October 2007 for cash as second tranche of placement	20,000,000	3,000,000	–	–
Issued on 15 November 2007 for cash as second tranche of placement	20,000,000	3,000,000	–	–
Issued on 16 and 19 June 2008 for cash – rights issue	77,793,460	5,445,542	–	–
Transaction costs on share issue	–	(226,032)	–	(366,726)
End of the financial year	291,724,429	46,914,438	173,930,969	35,694,928

	NUMBER OF WARRANTS	$	NUMBER OF WARRANTS	$
Warrants				
Beginning of the financial year	800	1,379,200	800	1,379,200
Issued during the year	–	–	–	–
End of the financial year	800	1,379,200	800	1,379,200

For the year ended 30 June 2008

12. Contributed Equity and Reserves continued

(c) Share Options

Employee Options

During the financial year Sunshine Heart, Inc. issued 691,000 options over ordinary shares with an issue term of 10 years. The options had an average exercise price of $0.30 and average vesting period of three years. During the year 7,605,858 options were cancelled or forfeited including 6,446,000 options where performance milestones were not achieved.

At the end of the year there were 19,895,344 (2007: 26,810,202) unissued ordinary shares in respect of which employee options were outstanding as remuneration to directors, consultants and employees of the Company (refer Note 15).

Placement Options

During the financial year Sunshine Heart, Inc. issued 16,000,000 options over ordinary shares with an issue term of 3 years as part of tranche 2 of the capital raising. These options were issued on 1 October 2007 (10,000,000) and 15 November 2007 (6,000,000) and had an exercise price of $0.20.

At the end of the year there were 43,604,079 (2007: 27,604,079) unissued ordinary shares in respect of which placement options were outstanding.

(d) Terms and conditions of contributed equity

Ordinary shares

Holders of shares have the right to receive dividends as and when declared and, in the event of a winding up of the Company, to participate in proceeds from the sale of all surplus assets in proportion to the number of and amounts paid up on shares held. Shares entitle their holder to one vote, either in person or by proxy, at a meeting of the Company.

Warrants

Warrants to purchase ordinary shares were issued in connection with an $800,000 29 June 2004 convertible promissory notes issued as a bridging loan prior to the Initial Public Offer. These warrants were issued to related party entities affiliated with directors Dr Geoff Brooke, Crispin Marsh and Dr William Peters and to one unrelated party. The Warrants entitle the holders to subscribe for a total of 3,200,000 shares at $0.25. The warrants have an exercise period of ten years and expire on 20 June 2014. No warrants were exercised during the year.

	CONSOLIDATED		SUNSHINE HEART, INC.	
	2008	2007	2008	2007
	$	$	$	$
(e) Accumulated Losses				
Movement in accumulated losses were as follows:				
Balance 1 July	**(30,215,208)**	(18,675,795)	**(30,215,208)**	(18,675,795)
Net loss attributable to members of Sunshine Heart, Inc.	**(9,738,183)**	(11,539,413)	**(9,738,183)**	(11,539,413)
Balance 30 June	**(39,953,391)**	(30,215,208)	**(39,953,391)**	(30,215,208)

(f) Reserves

Movement in reserves were as follows:

	CONSOLIDATED		SUNSHINE HEART, INC.	
	EMPLOYEE EQUITY BENEFITS RESERVE	TOTAL	EMPLOYEE EQUITY BENEFITS RESERVE	TOTAL
At 1 July 2006	**945,068**	945,068	**945,068**	945,068
Share-based payments	**319,760**	319,760	**319,760**	319,760
At 30 June 2007	**1,264,828**	1,264,828	**1,264,828**	1,264,828
Share-based payments	**329,827**	329,827	**329,827**	329,827
At 30 June 2008	**1,594,655**	1,594,655	**1,594,655**	1,594,655

(g) Dividends

No dividends were paid or recommended to be paid during the year (2007: Nil).

For the year ended 30 June 2008

	NOTES	CONSOLIDATED 2008 $	CONSOLIDATED 2007 $	SUNSHINE HEART, INC. 2008 $	SUNSHINE HEART, INC. 2007 $
13. Cash and Cash Equivalents					
(a) Reconciliation of the net loss after tax to the net cash flows from operations					
Net loss		**(9,738,183)**	(11,539,413)	**(9,738,183)**	(11,539,413)
Non-Cash Items					
Write down of investments in subsidiaries	3(b)	**–**	–	**9,357,218**	11,243,813
Depreciation and amortisation of non-current assets	3(c)	**78,277**	64,269	**–**	–
Loss on disposal of non-current assets		**36,796**	–	**–**	–
Share based payments expense		**329,827**	319,760	**–**	–
Unrealised net foreign exchange differences		**4,644**	77,408	**4,644**	77,408
Changes in assets and liabilities					
(Increase)/decrease in prepayments and other receivables		**150,984**	1,316,682	**(9,867)**	13,873
(Decrease)/increase in trade and other payables		**(36,795)**	(264,106)	**(78,263)**	(15,396)
Increase in provisions		**22,588**	27,908	**–**	–
Net cash outflow from operating activities		**(9,151,862)**	(9,997,492)	**(464,451)**	(219,715)
(b) Reconciliation of cash					
Cash balance comprises:					
– cash at bank		**2,320,313**	2,878,884	**1,446,537**	408,812
– term deposits		**7,452,304**	4,839,614	**7,452,304**	4,839,614
Closing cash balance		**9,772,617**	7,718,498	**8,898,841**	5,248,426
(c) Non-cash financing and investing activities					
Share based payments		**329,827**	319,760	**–**	–

(d) Terms and conditions

For the purposes of the cash flow statement, cash comprises short term deposits with an original maturity of three months or less and cash at bank.

14. Commitments

	CONSOLIDATED 2008 $	CONSOLIDATED 2007 $	SUNSHINE HEART, INC. 2008 $	SUNSHINE HEART, INC. 2007 $
(a) Lease expenditure commitments – Group as lessee				
(i) Operating leases (non-cancellable)				
Minimum lease payments				
– not later than one year	**176,850**	105,165	**–**	–
– later than one year and not later than five years	**136,379**	–	**–**	–
Aggregate lease expenditure contracted for at reporting date	**313,229**	105,165	**–**	–

Operating lease expenditure commitments include two property leases. The St Leonards property lease expires on 31 March 2010. The Orange County, California property lease expires on 2 April 2010. Both property leases are expected to be renewed on similar terms at expiration.

(b) Other expenditure commitments				
Commitments contracted for at reporting date but not recognised as liabilities are as follows:				
– not later than one year	**387,916**	81,897	**–**	–
– later than one year and not later than five years	**–**	–	**–**	–
Aggregate other expenditure contracted for at reporting date	**387,916**	81,897	**–**	–

15. Share-based Payments Plan

Employee Share Incentive Scheme

The 2002 Stock Plan ("the Plan") has been established, pursuant to which Sunshine Heart may, at the discretion of the Board or a committee appointed by the Board to administer the Plan, grant options to purchase Shares of Sunshine Heart to directors, employees, advisors and consultants ("employees") of the consolidated entity. The options are issued for a term stated in the option agreement, not exceeding ten years from the date of the grant. The options are not quoted on the ASX.

At 30 June 2008 there were 11 retained Key Management Personnel and 7 staff members eligible for the Plan. Any vesting requirements are set out in the option agreements and are determined at the discretion of the Board or a Board-appointed administration committee.

Information with respect to the number of options granted under the Plan is as follows. It is noted that where the exercise price is dominated in US dollars, it has been translated to Australian dollars using the exchange rate applicable on 30 June 2008, being $0.9615. All options issued and outstanding under the Plan do not carry dividend and/or voting rights.

For the year ended 30 June 2008

15. Share-based Payments Plan continued

	2008		2007	
	NUMBER OF OPTIONS	WEIGHTED AVERAGE EXERCISE PRICE	NUMBER OF OPTIONS	WEIGHTED AVERAGE EXERCISE PRICE
	$	$	$	$
Balance at beginning of year	**26,810,202**	**0.26**	11,817,418	0.25
– granted	**691,000**	**0.30**	15,398,784	0.27
– cancelled	**(1,104,858)**	**0.39**	(406,000)	0.39
– forfeited	**(6,501,000)**	**0.28**	–	–
Balance at end of year	**19,895,344**	**0.24**	26,810,202	0.26

Options held as at the end of the reporting period

The following table summarises information about options held by the employees as at 30 June 2008. The options granted do not provide dividend and or voting rights. No consideration was paid to the entity from employees on granting of the options.

NUMBER OF OPTIONS	GRANT DATE	VESTING	EXPIRY DATE	WEIGHTED AVERAGE EXERCISE PRICE
				$
2,033,238	19 Dec 02 to 13 Oct 03	19 Dec 02 to 1 Nov 03	18 Dec 12 to 12 Oct 13	0.01
1,783,282	31 Jan 03	31 Jan 03	30 Jan 13	0.07
38,800	29 Apr 03	31 Jan 03	28 Apr 13	0.12
795,400	19 May 04	30 Mar 04	18 May 14	0.08
3,691,490	23 Jun 04	28 Sep 04	23 Jun 14	0.28
485,000	20 Jul 04	28 Sep 04	20 Jul 14	0.50
19,400	31 May 05	31 May 05	30 May 10	0.60
179,000	21 Jun 05	10 Jan 05 to 21 Jun 05	20 June 10	0.48
909,000	9 Feb 06	7 Nov 05 to 3 Jan 06	8 Feb 16	0.35
330,417	21 Apr 06	31 Mar 06	20 Apr 16	0.37
58,200	2 Jun 06	1 Jun 06	1 Jun 16	0.25
1,338,784	1 Nov 06	1 Nov 06	31 Oct 16	0.20
2,016,333	31 Jan 07	31 Jan 07	30 Jan 07	0.29
1,690,000	16 Apr 07	30 Jun 07	15 Apr 17	0.30
3,786,000	18 Apr 07	30 Jun 07	17 Apr 17	0.30
50,000	24 May 07	24 May 07	23 May 17	0.20
400,000	10 Oct 07	10 Oct 08	9 Oct 17	0.30
291,000	18 Dec 07	18 Dec 08	18 Dec 17	0.30

Options granted as part of employee remuneration have been valued using the Black-Scholes option pricing methodology, to provide the fair value of the options. This methodology takes into account factors such as the share price at grant date, the exercise price, the term of the option, the expected price volatility of the underlying share, the expected dividend yield and the risk-free interest rate for the term of the option. With regards to the performance conditions, options to individuals are assumed to vest, and therefore it is not appropriate to reduce fair value estimates of options that may not vest.

Fair value of options

The fair value of each option is estimated on the grant date using a Black-Scholes option pricing model with the following weighted average assumptions used:

	2008	2007
Dividend yield (%)	**0%**	0%
Risk-free Interest rate (%)	**6.33%**	6.10%
Expected volatility (%)	**45%**	45%
Expected life of option (years)	**5 years**	5 years
Weighted average exercise price	**$0.26**	$0.26

Historical data is used as the main component to determine expected volatility.

The amount of options remuneration is determined on a pro-rata basis, by amortising the fair value estimate of each option, over the vesting period of the individual option grant. The fair value of options granted as compensation is recognised as an expense on a pro-rata basis over the vesting period in the income statement with a corresponding adjustment to equity.

Weighted average fair value

The weighted average fair value of options granted during the year was $0.09 (2007: $0.09)

Weighted average remaining contractual life

The weighted average remaining contractual life for the share options outstanding as at 30 June 2008 is 7.18 years (2007: 8.16 years).

16. Contingent Liabilities

Commercial Ready Grant

On 21 October 2005, Sunshine Heart Company Pty Limited (SHCP) received a Commercial Ready Grant from the Australian Government through AusIndustry. The grant contributed fifty cents for each dollar spent on eligible project spends, to a maximum funding of $2.23 million.

On 13 June 2006, SHCP received a further Commercial Ready Grant from the Australian Government through AusIndustry. The grant contributes fifty cents for each dollar spent on eligible project spends, to a maximum funding of $2.16 million.

Under the terms of both agreements, the government may require SHCP to repay all or some of the amount, including interest, in any of the following circumstances:

(a) SHCP fails to use its best endeavours to commercialise the relevant grant project within a reasonable time of completion of the project; or

(b) Upon termination of a grant due to breach or insolvency; or

(c) At any time for up to five years, a change in control occurs whereby either Sunshine Heart, Inc.'s ownership of the subsidiary (grant recipient) falls below fifty percent or Australian ownership of Sunshine Heart, Inc falls below fifty per cent.

SHCP continues the development and commercialisation of all projects funded by the Commercial Ready program. The total amount received under the Commercial Ready Programs as at 30 June 2008 was $4.07 million.

17. Subsequent Events

There were no material events occurring after balance date which may affect either the Group's operations or results of those operations or the Group's state of affairs.

For the year ended 30 June 2008

18. Earnings Per Share

	2008 $	2007 $
The following reflects the income and share data used in the calculations of basic and diluted loss per share:		
Net loss	(9,738,183)	(11,539,412)
Weighted average number of ordinary shares used in calculating basic and dilutive earnings per share (Note that, had the dilutive shares been factored, this would have reduced the net loss per share):	204,203,178	139,142,250

The following type and number of shares are not included in the weighted average number of ordinary shares noted above as they are anti-dilutive in nature:

– Warrants 3,200,000

– Options 60,499,423

19. Auditors' Remuneration

	CONSOLIDATED		SUNSHINE HEART, INC.	
	2008 $	2007 $	2008 $	2007 $
Amounts received or due and receivable by Ernst & Young Australia for:				
– an audit or review of the financial report of the entity and any other entity in the consolidated entity	**111,662**	128,780	**111,662**	128,780
– an audit or review of the financial report of the entity and any other entity in the consolidated entity that relates to prior year	**–**	34,880	**–**	34,880
– other services in relation to the entity and any other entity in the consolidated entity				
- Tax compliance services	**8,383**	23,372	**–**	14,022
- Advisory services	**17,140**	2,500	**–**	–
	137,185	189,532	**111,662**	177,682

20. Director and Executive Disclosures

(a) Details of Key Management Personnel

Directors

Mr Malcolm McComas	Chairman (non-executive)
Dr Geoff Brooke	Director (non-executive)
Dr Richard Lin	Director (non-executive) *(resigned 15 November 2007)*
Mr Crispin Marsh	Director (non-executive)
Mr Donal O'Dwyer	Director (non-executive)
Dr William Peters	Medical Director and Chief Technology Officer
Mr John Brennan	Director (non-executive)
Mr Donald Rohrbaugh	Chief Executive Officer
Dr Conrad Wang	Director(non-executive) *(appointed 15 November 2007, resigned 10 July 2008)*
Mr Nicholas Callinan	Director (non-executive) *(appointed 10 July 2008)*

Executives

Mr Victor Windeyer	Chief Operating Officer
Mr Brian Bolton	Chief Financial Officer and Company Secretary
Mr Gary Frugard	VP of Regulatory and Quality Affairs to 26 March 2008
Ms Mary Beth Kepler	VP of Regulatory and Quality Affairs from 26 March 2008

(b) Compensation of Key Management Personnel

	CONSOLIDATED		SUNSHINE HEART, INC.	
	2008	2007	2008	2007
	$	$	$	$
Short-Term	**1,566,820**	1,450,617	**175,000**	200,719
Post Employment	**39,996**	24,467	**–**	–
Share-based Payment	**301,815**	256,266	**5,688**	12,143
Long-Term	**–**	–	**–**	–
	1,908,631	1,731,350	**180,688**	212,862

Sunshine Heart, Inc. has applied the option under Corporations Amendments Regulation 2007 to transfer Key Management Personnel remuneration disclosures required by AASB 124 Related Party Disclosures paragraphs Aus 25.4 to Aus 25.7.2 to the Remuneration report section of the Directors' report. These transferred disclosures have been audited.

For the year ended 30 June 2008

20. Director and Executive Disclosures continued

(c) Option holdings of Key Management Personnel

June 2008

	BALANCE AT BEGINNING OF PERIOD 1 JULY 2007	GRANTED UNDER CAPITAL RAISING, SEE NOTE	OPTIONS FORFEITED *	BALANCE AT END OF PERIOD 30 JUNE 2008	VESTED AT 30 JUNE 2008 NOT EXERCISABLE	VESTED AND EXERCISABLE
Directors						
M McComas	388,000	–	–	388,000	–	388,000
G Brooke (1)	8,497,000	7,466,667	–	15,963,667	–	15,963,667
R Lin/C Wang (2)	2,116,400	–	–	2,116,400	2,000,000	116,400
C Marsh	2,106,665	–	–	2,106,665	1,156,349	950,316
D O'Dwyer	97,000	–	–	97,000	–	97,000
W Peters	4,013,881	–	(1,344,000)	2,669,881	690,833	1,979,048
J Brennan (3)	9,600,000	8,533,333	–	18,133,333	–	18,133,333
D Rohrbaugh	9,574,923	–	(1,920,000)	7,654,923	2,197,408	5,457,515
Executives						
V Windeyer	2,840,000	–	(960,000)	1,880,000	937,500	942,500
B Bolton	1,800,000	–	(110,000)	1,690,000	1,080,208	609,792
G Frugard	1,141,490	–	(340,800)	800,690	180,625	620,065
M Kepler	550,000	–	(264,000)	286,000	166,146	119,854
Total	42,725,359	16,000,000	(4,938,800)	53,786,559	8,409,069	45,377,490

* Options forfeited due to milestones not being achieved.

No options were exercised during the year.

June 2007

	BALANCE AT BEGINNING OF PERIOD 1 JULY 2007	GRANTED UNDER CAPITAL RAISING, SEE NOTE	OPTIONS FORFEITED *	BALANCE AT END OF PERIOD 30 JUNE 2008	VESTED AT 30 JUNE 2007 NOT EXERCISABLE	VESTED AND EXERCISABLE
Directors						
M McComas	388,000	–	–	388,000	–	388,000
G Brooke [1]	97,000	–	8,400,000	8,497,000	8,400,000	97,000
R Lin [2]	116,400	–	2,000,000	2,116,400	2,000,000	116,400
C Marsh	797,881	308,784	1,000,000	2,106,665	1,258,784	847,881
D O'Dwyer	97,000	–	–	97,000	–	97,000
W Peters	1,573,881	2,440,000	–	4,013,881	2,749,801	1,264,080
J Brennan [3]	–	–	9,600,000	9,600,000	9,600,000	–
D Rohrbaugh	3,934,923	5,640,000	–	9,574,923	7,001,389	2,573,534
Executives						
V Windeyer	800,000	2,040,000	–	2,840,000	2,493,333	346,667
B Bolton	–	1,800,000	–	1,800,000	1,789,000	11,000
A Blunden	350,000	–	–	350,000	35,417	314,583
G Frugard	506,490	635,000	–	1,141,490	819,067	322,423
Total	8,661,575	12,863,784	21,000,000	42,525,359	36,146,791	6,378,568

1 Options issued to GBS Venture Partners Limited in its capacity as manager and trustee of the GBS Bioventures II and III Trusts. Dr G Brooke has an indirect interest as a member and the Managing Director of GBS Venture Partners Limited.

2 Options issued to Three Arch Management III L.P. Dr C Wang is an associate and Dr R Lin a member.

3 Options issued to CM Capital Investments in its capacity as trustee of CM Capital Venture Trust 4A and CM Capital Venture Trust 4B. Mr J Brennan has an indirect interest as a member and Partner of CM Capital Investments.

(d) Ordinary Shareholdings of Key Management Personnel in Sunshine Heart, Inc.

	BALANCE 1 JULY 2006	PURCHASED 1 JULY 2006 TO 30 JUNE 2007	BALANCE 30 JUNE 2007	PURCHASED/SOLD 1 JULY 2007 TO 30 JUNE 2008	BALANCE 30 JUNE 2008
Directors					
M McComas	100,000	–	100,000	36,364	136,364
G Brooke [1]	13,184,835	28,000,000	41,184,835	50,963,074	92,147,909
C Wang/R Lin [2]	9,205,801	6,666,667	15,872,468	–	15,872,468
C Marsh	3,930,235	3,333,333	7,263,568	735,714	7,999,282
D O'Dwyer	305,000	320,000	625,000	–	625,000
W Peters	7,001,161	–	7,001,161	500,000	7,501,161
J Brennan [3]	–	32,000,000	32,000,000	50,112,479	82,112,479
Executives					
B Bolton	–	–	–	290,608	290,608
V Windeyer	28,825	–	28,825	71,429	100,254
Total	33,755,857	70,320,000	104,075,857	102,709,668	206,785,525

1 Shares are held by GBS Venture Partners Limited in its capacity as manager and trustee of the GBS Bioventures II and III Trusts. Dr G Brooke has an indirect interest as a member and the Managing Director of GBS Venture Partners Limited.

2 809,816 shares are held by Three Arch Associates III LP and 15,052,652 shares held by Three Arch Partners III LP. Dr C Wang is an associate (2007: Dr R Lin a member) of the general partner of each entity, Three Arch Management III, LLC.

3 32,000,000 shares are held by CM Capital Investments. Mr J Brennan has an indirect interest as a member and Partner of CM Capital Investments

(e) Other transactions and balances with Key Management Personnel

During the year ended 30 June 2008, Sunshine Heart Company Pty Limited paid $27,125 (2007: $13,219) to SCP Technology and Growth Pty Limited, a company controlled by C Marsh, for the provision of intellectual property and patent services. As at 30 June 2008, there were no monies outstanding with Key Management Personnel (2007: $nil).

For the year ended 30 June 2008

21. Related Party Disclosures

(a) Ultimate parent

Sunshine Heart, Inc. (incorporated in Delaware, USA) is the ultimate parent entity.

The following related party transactions occurred with the wholly-owned group during the financial year:

During the year ended 30 June 2008, Sunshine Heart, Inc. subscribed for an additional 7,000,000 ordinary fully paid shares in Sunshine Heart Company Pty Limited. The cost of acquisition was $7,000,000. Furthermore, Sunshine Heart, Inc. made additional non-cash investments into its wholly owned subsidiary during the year in recognition of the share based payments expense (options remuneration) of $329,827 (2007: $319,760), refer Note 12.

All transactions with Key Management Personnel other than those arising from the exercise of remuneration options have been entered into under terms and conditions no more favourable than those the entity would have adopted if dealing at arm's length.

(b) Other related parties

During the year ended 30 June 2008 Sunshine Heart, Inc. paid GBS Venture Partners and CM Capital Investments underwriting fees of $86,387 and $76,978 respectively, being equal to 3% of the sum of monies underwritten by each party as part of the rights issue completed on 19 June 2008.

22. Segment Information

(a) Segment products and locations

The consolidated entity operates in one industry segment, which is the research and development of heart assist devices, and in two geographical segments, which are Australia and the United States.

(b) Segment accounting policies

Segment accounting policies are the same as the consolidated entity policies described in Note 2. During the year there have been no changes in segment accounting policies that had a material effect on the segment information.

(c) Geographic Segments

2008	AUSTRALIA	UNITED STATES	UNALLOCATED	ELIMINATION	CONSOLIDATION
	$A	$A	$A	$A	$A
Segment Revenue	–	–	441,121	–	441,121
Segment Results	(9,738,183)	(10,186,254)	441,121	9,357,218	(10,126,099)
Other segment information:					
Depreciation	63,289	–	–	–	63,289
Amortisation	14,988	–	–	–	14,988
Investments write-down	–	9,357,218	–	(9,357,218)	–
Segment assets	10,120,593	515,842	32,800	(490,781)	10,178,454
Segment liabilities	629,770	1,703	–	–	631,473
Acquisition of plant and equipment	8,885	–	–	–	8,885
Net Cash flow information:					
Used in operating activities	(7,358,369)	(2,216,099)	422,611	–	(9,151,857)
Used in investing activities	(8,885)	–	–	–	(8,885)
From financing activities	11,219,505	–	–	–	11,219,505

All non current assets are located in Australia.

2007	AUSTRALIA	UNITED STATES	UNALLOCATED	ELIMINATION	CONSOLIDATION
	$A	$A	$A	$A	$A
Segment Revenue	2,694,224	–	526,498	–	3,220,722
Segment Results	(11,709,932)	(11,940,830)	526,498	11,243,813	(11,539,413)
Other segment information:					
Depreciation	55,747	–	–	–	55,747
Amortisation	8,522	–	–	–	8,522
Investments write-down	–	11,243,813	–	(11,243,813)	–
Segment assets	8,362,200	2,953,651	14,290	(2,948,634)	8,381,507
Segment liabilities	177,805	79,954	–	–	257,759
Acquisition of plant and equipment	174,246	–	–	–	174,246
Net Cash flow information:					
Used in operating activities	(9,827,820)	(697,017)	527,345	–	(9,997,492)
Used in investing activities	(174,246)	–	–	–	(174,246)
From financing activities	13,435,670	–	–	–	13,435,670

23. FINANCIAL INSTRUMENTS

(a) Financial risk management objectives and policies

The Board determines and regularly reviews the Group's financial instrument policy and performance. The Group's principal financial instruments comprise cash and short-term bank deposits. The Group does not utilise derivatives, holds no debt and does not trade in financial instruments. The Group has other financial assets and liabilities such as other receivables and other payables, which arise directly from its operations.

The main risks arising from the Group's financial instruments are foreign currency risk and liquidity risk. The Board policies for managing these risks are summarised below.

Details of the significant accounting policies and methods adopted, including the criteria for methods adopted, including the criteria for recognition, the basis of measurement and the basis on which income and expenses are recognised, in respect of each class of financial asset, financial liability and equity instrument are disclosed in Note 2 to the financial statements.

Interest rate risk

The Group is only exposed to interest rate risk in the area of cash at bank as it has no borrowings.

Credit risk management

Credit risk arises from the cash and cash equivalents of the Group. Credit risk refers to the risk that a counterparty will default on its contractual obligations resulting in financial loss to the Group. The consolidated entity measures credit risk on a fair value basis.

For the year ended 30 June 2008

23. Financial Instruments continued

(b) Risk exposures and responses

The credit risk on liquid funds is limited because the counterparties are banks with high credit-ratings assigned by international credit-rating agencies.

The carrying amount of financial assets recorded in the financial statements, net of any allowances for losses, represents the consolidated entity's maximum exposure to credit risk without taking account of the value of any collateral obtained.

At balance date, the Group has the following financial assets (no financial liabilities at 30 June 2008 or 30 June 2007) exposed to Australian variable interest rate not designated in cash flow hedges:

	CONSOLIDATED		SUNSHINE HEART, INC.	
	2008	2007	2008	2007
	$	$	$	$
Financial Assets				
Cash and cash equivalents	**9,772,617**	7,718,498	**8,998,841**	5,248,426
	9,772,617	7,718,498	**8,998,841**	5,248,426

The following sensitivity analysis is based on the interest rate risk exposures in existence at the balance sheet date. At 30 June 2008, if interest rates moved, as illustrated in the table below, with all other variables held constant, post tax profit and equity would have been affected as follows:

	POST TAX PROFIT HIGHER/(LOWER)		EQUITY HIGHER/(LOWER)	
	2008	2007	2008	2007
	$	$	$	$
Consolidated				
+1% (100 basis points)	**97,726**	77,184	**97,726**	77,184
-0.5% (50 basis points)	**(48,863)**	(38,592)	**(48,863)**	(38,592)
Parent				
+1% (100 basis points)	**89,988**	52,484	**89,988**	52,484
-0.5% (50 basis points)	**(44,994)**	(26,242)	**(44,994)**	(26,242)

The movements in profit are due to the higher/lower interest income from variable rate term deposits and cash balances. There is no equity movement as there are no financial assets or financial liabilities which are designated as cash flow hedges.

Foreign Currency Risk

The Group is exposed to a small amount of foreign currency risk as a result of holding a US bank account and paying some expenses in US dollars. The Group did not seek to hedge this exposure in the current or prior year, primarily due to the uncertainty of the magnitude and timing of foreign denominated expenses being incurred. Where the Group can reasonably forecast likely future US Dollar denominated expenses being incurred in advance, it may consider holding a similar magnitude of funds in the US dollar bank account for ease of administration. The Board reviews the ongoing appropriateness of the Group's policy on managing foreign currency risk based on the level of foreign operations.

At 30 June 2008, the group had the following exposure to US$ foreign currency that is not designated in cash flow hedges:

	CONSOLIDATED		SUNSHINE HEART, INC.	
	2008	2007	2008	2007
	$	$	$	$
Financial Assets				
Cash and cash equivalents	**25,062**	47,565	**25,062**	47,565
Financial Liabilities				
Sundry creditors	**472,790**	1,127	**472,790**	1,127

Net exposure

The following sensitivity is balance on the foreign currency risk exposures in existence at the balance sheet date. At 30 June 2008, had the Australian dollar moved, as illustrated in the table below, with all other variables held constant post tax profit and equity would have been affected as follows:

	POST TAX PROFIT HIGHER/(LOWER)		EQUITY HIGHER/(LOWER)	
	2008	2007	2008	2007
	$	$	$	$
Consolidated and Parent				
AUS/USD +10%	**42,630**	4,869	**42,630**	4,869
AUS/USD -5%	**(24,898)**	(2,435)	**(24,893)**	(2,435)

Management believe the balance date risk exposures are representative of the risk exposure inherent in the financial instruments.

Liquidity risk exposure

The Group's objective is to maintain a balance between continuity of funding for meeting its operating costs and maximising financing revenue through at call bank deposits in line with budget requirements. The Group's policy is to minimise its forward commitments in achieving this objective.

All liquid assets are less than 60 days represented by cash and cash equivalents, other current assets and other receivables.

All liquid liabilities contractual maturities are less than 60 days represented by trade and other payables. The contractual maturity amounts are the current carrying value.

The group monitors its liquidity by reviewing a 12 month rolling forecast in conjunction with its overall strategy.

Fair value of financial instruments

The fair value of assets and liabilities approximates the carrying amount.

Capital Management

When managing capital, the Board's objective is to ensure the Company continues as a going concern and to optimise the returns to shareholders and benefits to other stakeholders. The Company is in early stage development and its primary source of funding is via the equity market. The Company continually reviews market trends and the impact that this may have on the capital markets and the ability to raise capital when managing its risk cashflow. During the year the Company raised $9.4 million and further details are contained in Note 12(b). The directors will continue to raise capital as and when needed to meet its ongoing capital commitments.

Directors' Declaration

In accordance with a resolution of the directors of Sunshine Heart, Inc. I state that:

In the opinion of the directors:

(a) the financial statements and notes of the Company and the consolidated entity are in accordance with the Corporations Act 2001, including:

   (i) giving a true and fair view of the Company's and consolidated entity's financial position as at 30 June 2008 and of their performance for the year ended on that date; and

   (ii) complying with Accounting Standards and the Corporations Regulations 2001; and

(b) there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.

(c) this declaration has been made after receiving the declarations required to be made to the Directors in accordance with section 295A of the Corporations Act 2001 for the financial year ending 30 June 2008.

On behalf of the Board

D.G. Rohrbaugh

Donald Rohrbaugh
Director
Sydney, 21 August 2008

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Auditor's Independence Declaration to the Directors of Sunshine Heart, Inc

In relation to our audit of the financial report of Sunshine Heart, Inc for the financial year ended 30 June 2008, to the best of my knowledge and belief, there have been no contraventions of the auditor independence requirements of the Corporations Act 2001 or any applicable code of professional conduct.

Ernst & Young

Ernst & Young

Gamini Martinus

Gamini Martinus
Partner
Sydney
21 August 2008

Independent Audit Report

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Independent auditor's report to the members of Sunshine Heart, Inc.

Report on the Financial Report

We have audited the accompanying financial report of Sunshine Heart, Inc., which comprises the balance sheet as at 30 June 2008, and the income statement, statement of recognised income and expense and cash flow statement for the year ended on that date, a summary of significant accounting policies, other explanatory notes and the directors' declaration of the consolidated entity comprising the company and the entity it controlled at the year's end or from time to time during the financial year.

Directors' Responsibility for the Financial Report

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

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial report. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the financial report, whether due to fraud or error. In making those risk assessments, we consider internal controls relevant to the entity's preparation and fair presentation of the financial report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal controls. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial report.

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

Independence

In conducting our audit we have met the independence requirements of the *Corporations Act 2001*. We have given to the directors of the company a written Auditor's Independence Declaration, a copy of which is included on Page 59. In addition to our audit of the financial report, we were engaged to undertake the services disclosed in the notes to the financial statements. The provision of these services has not impaired our independence.

Auditor's Opinion

In our opinion:

1. the financial report of Sunshine Heart, Inc. is in accordance with the *Corporations Act 2001*, including:

   i giving a true and fair view of the financial position of Sunshine Heart, Inc. and the consolidated entity at 30 June 2008 and of their performance for the year ended on that date; and

   ii complying with Australian Accounting Standards (including the Australian Accounting Interpretations) and the *Corporations Regulations 2001*.

2. the financial report also complies with International Financial Reporting Standards as issued by the International Accounting Standards Board.

Inherent Uncertainty Regarding Continuation of Going Concern

Without qualification to the opinion expressed above, attention is drawn to the following matter. As a result of the matters described in Note 2 (c) "Going Concern" to the financial statements, there is significant uncertainty whether the company and/or the consolidated entity will be able to continue as going concerns and therefore whether they will be able to pay their debts as and when they fall due and realise their assets and extinguish their liabilities in the normal course of business and at the amounts stated in the financial report. The financial report does no include any adjustments relating to the recoverability and classification of recorded asset amounts or to the amounts and classification of liabilities that might be necessary should the company and/or the consolidated entity not continue as going concerns.

Report on the Remuneration Report

We have audited the Remuneration Report included in pages 13 to 18 of the directors' report for the year ended 30 June 2008. The directors of the company are responsible for the preparation and presentation of the Remuneration Report in accordance with section 300A of the *Corporations Act 2001*. Our responsibility is to express an opinion on the Remuneration Report, based on our audit conducted in accordance with Australian Auditing Standards.

Auditor's Opinion

In our opinion the Remuneration Report of Sunshine Heart, Inc. for the year ended 30 June 2008, complies with section 300A of the *Corporations Act 2001.*

Ernst & Young

Ernst & Young

Gamini Martinus

Gamini Martinus
Partner
Sydney
21 August 2008

ASX Additional Information

Additional information required by the Australian Stock Exchange Ltd and not shown elsewhere in this report is as follows.

For the purposes of this report, Chess Depository Instrument (CDI) holders and certificated shareholders are shown as one class of shareholder, notwithstanding CDI holders having beneficial interests in the underlying shares, rather than legal title.

Chess Depository Nominees Pty Ltd (CDN) as a subsidiary of the Australian Stock Exchange Ltd holds the legal title in the Company's shares, for and on behalf of CDI holders, to effect broker-to-broker settlement of trading in the underlying shares. Holders of CDIs are entitled to all the economic benefits of the underlying shares as though they were holders of the legal title. For the purposes of the information below, CDN has been excluded and the terms CDI/fully paid ordinary shares or shares are interchangeable.

This information is current as at 18 August 2008.

(a) Distribution of equity securities

(i) Ordinary share capital

- 291,724,429 fully paid ordinary shares are held by 800 individual security holders.

CDI holders are not entitled to vote at shareholder meetings as CDN holds legal title to the Company's shares, for and on their behalf. CDI holders should direct CDN on how to vote on proposed resolutions at shareholder meetings. CDN must exercise its right to vote by proxy at shareholder meetings in accordance with the directions of CDI holders.

All issued ordinary shares carry one vote per share without restriction.

(ii) Warrants

- 3,200,000 unquoted warrants over ordinary shares are held by 4 individual security holders. Warrants do not carry a right to vote.

(iii) Options

- 63,499,423 unquoted options over ordinary shares are held by 53 individual security holders. Options do not carry a right to vote.

The number of security holders, by size of holding, in each class are:

	FULLY PAID ORDINARY SHARES	WARRANTS	OPTIONS
1 – 1,000	7	–	–
1,001 – 5,000	119	–	4
5,001 – 10,000	186	–	3
10,001 – 100,000	379	–	45
100,001 and over	109	4	40
	800	4	92
Holding less than a marketable parcel of shares are:	321	–	–

(b) Substantial shareholders

ORDINARY SHAREHOLDERS	FULLY PAID NUMBER	PERCENTAGE
GBS Venture Partners Limited (GBS Bioventures III A/C)	55,986,769	19.19
GBS Venture Partners Limited (GBS Bioventures II A/C)	20,000,000	12.40
Australian Executor Trustees Ltd (CM Capital Venture 4A A/C)	16,000,000	9.09
Australian Executor Trustees Ltd (CM Capital Venture 4B A/C)	16,000,000	9.09
Three Arch Partners III LP	15,062,652	5.16

(c) Twenty largest holders of quoted equity securities

ORDINARY SHAREHOLDERS	FULLY PAID NUMBER	PERCENTAGE
Ordinary shareholders		
GBS Venture Partners Limited (GBS Bioventures III A/C)	55,986,769	19.19
GBS Venture Partners Limited (GBS Bioventures II A/C)	36,161,140	12.40
Australian Executor Trustees Ltd (CM Capital Venture 4A A/C)	26,510,785	9.09
Australian Executor Trustees Ltd (CM Capital Venture 4B A/C)	26,510,785	9.09
Three Arch Partners III LP	15,062,652	5.16
CM Capital VT4A Pty Ltd (CM Capital Venture 4A A/C)	14,545,455	4.99
CM Capital VT4A Pty Ltd (CM Capital Venture 4B A/C)	14,545,454	4.99
Phillip Asset Management Ltd (IB Aus Bioscience Fund I A/C)	11,835,679	4.06
J P Morgan Nominees Australia Limited	9,450,727	3.24
WSP Holdings Limited	5,061,161	1.73
Asia Union Investments Pty Ltd	5,003,000	1.71
HSBC Custody Nominees (Australia) Limited – A/C 2	3,961,687	1.36
PCLM Investments Pty Ltd	3,333,333	1.14
National Nominees Limited	3,225,000	1.11
Invia Custodian Pty Limited	3,000,000	1.03
Australian Biotechnology and Healthcare Fund No 3 Limited	2,672,889	0.92
The Australian National University	2,423,766	0.83
PCLM Investments Pty Ltd	2,239,383	0.77
Szigetvary Trustee Services Ltd	1,940,000	0.67
ANZ Nominees Limited	1,500,000	0.51
	244,969,665	83.97

Corporate Directory

ABN 79 109 440 888

Directors
Mr Malcolm McComas (Chairman)
Mr John Brennan
Dr Geoff Brooke
Mr Nicholas Callinan
Mr Crispin Marsh
Mr Donal O'Dwyer
Dr William Peters
Mr Donald Rohrbaugh (Chief Executive Officer)

Company Secretary
Mr Brian Bolton

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