

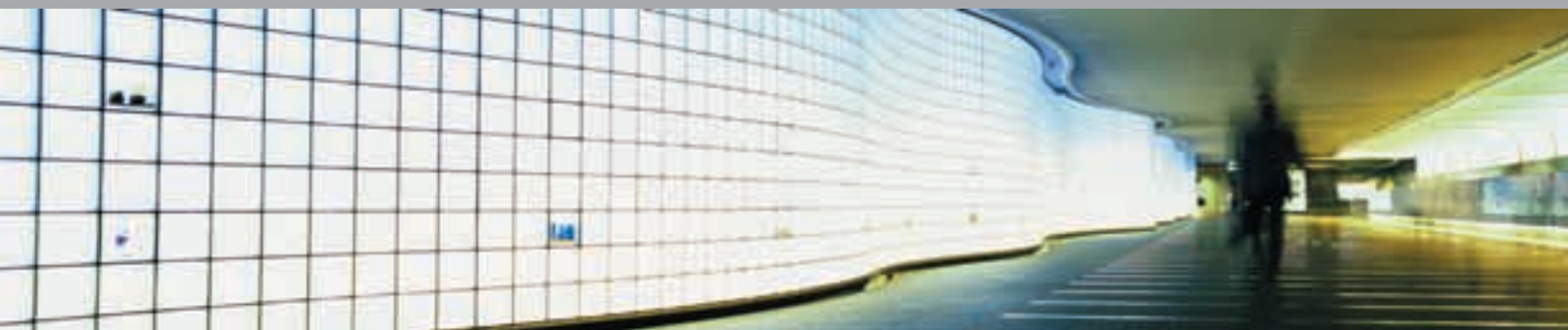
NEW DIRECTIONS

AMERICAN
SHARED
HOSPITAL
SERVICES

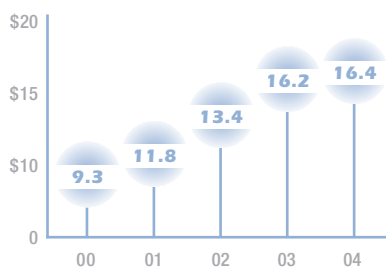
ANNUAL REVIEW 2004

TODAY, TOMORROW, AND BEYOND

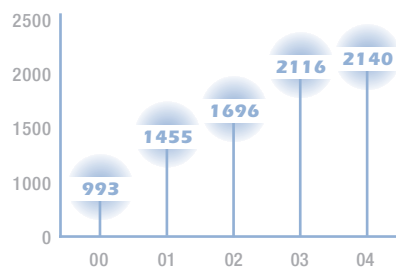
At American Shared Hospital Services, we view our achievements as a springboard for new directions. By expanding into new markets and exploring new technologies and partnerships, we continually reinvent ourselves, ensuring our success today, tomorrow, and beyond.



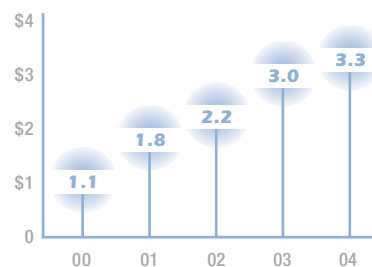
Gamma Knife Revenue
(\$ in Millions)



Gamma Knife
Procedures



Operating Income
(\$ in Millions)



NEW DIRECTIONS:

To Our Shareholders

In this annual report, you will read about some exciting new directions for American Shared Hospital Services. As our Gamma Knife business continues to thrive, we are actively pursuing new technological and partnering opportunities that will leverage our highly successful business model—bringing us to an even greater level of growth and success.

Looking back at fiscal 2004, I am pleased to report that our operating income reached an all-time high of \$3.3 million—a 10% increase over fiscal 2003. This was our fourth consecutive year of double-digit operating income increases. In addition, our Gamma Knife revenues totaled \$16.4 million, and our annual dividend payment of 16³/₄ cents reflected a 4.7% increase over fiscal 2003.

Turning to 2005, our key objectives are to continue our double-digit operating income growth and return to double-digit revenue growth. Our focus on increasing efficiency and reducing costs, which contributed to our record operating income for 2004, will continue. We also anticipate more rapid revenue growth in 2005, with one new Gamma Knife center already in operation this year and two more opening mid-year—bringing our total Gamma Knife facilities to 21.

However, we view this as only the beginning of a new era of growth for our company. Currently, we see three key areas for future growth. First, the advent of image-guided IMRT, which has given new life to our efforts to leverage our creative financing models to other technologies. Second, our Operating Room for the 21st Century® (OR21®) concept, which is rapidly becoming a reality—with suite design currently taking place. And third, our tax-exempt financing program.

These new directions, coupled with our strong market presence in the Gamma Knife arena, will give rise to our continuing success today, tomorrow, and beyond. I look forward to updating you on our progress in the coming years.

Ernest A. Bates, M.D. / Chairman and Chief Executive Officer / April 25, 2005

Innovative financing solutions

TODAY:

The Gamma Knife is the worldwide radiosurgical leader in the non-invasive treatment of malignant and benign brain tumors, vascular malformations, and trigeminal neuralgia. Patients who undergo this treatment have comparable or better outcomes, fewer complications, faster recoveries, and shorter hospital stays compared to an open neurosurgical procedure. To remain competitive and offer their patients the best possible treatment, hospitals everywhere want to offer this state-of-the-art technology. But they face tremendous obstacles in funding such an investment.

Since 1991, American Shared has offered institutions the financing solution that's right on target: our fee-per-use financing model. Through this innovative approach, they can open Gamma Knife centers quickly—without the worry of capital investment, fixed monthly payments, or technological obsolescence.

With our help, 19 Gamma Knife centers have opened throughout the country, at notable institutions such as The Johns Hopkins Hospital, Tufts-New England Medical Center, and University of California, San Francisco Medical Center. In 2005, we have already started a new center at Baptist Hospital of East Tennessee and have two more centers scheduled to open mid-year—at Northern Westchester Hospital in New York and Mercy Health Center in Oklahoma City.

More institutions turn to us for Gamma Knife financing than any other organization, making our market presence in this arena second-to-none. In fact, as of year-end 2004, we had installed 20% of the Gamma Knife units in the United States.

OUR GAMMA KNIFE OPERATING INCOME ROSE 10% IN 2004 – TO AN ALL-TIME HIGH OF \$3.3 MILLION.

A BUSINESS MODEL THAT WORKS—

FOR US, AND FOR OUR CUSTOMERS

MARKET PRESENCE

TOMORROW:

Intensity Modulated Radiation Therapy (IMRT) delivers radiation doses to selected parts of the body with incredible precision. With this technology, tumors can be targeted aggressively but risk to normal tissues and organs is substantially minimized.

Now, a new innovation—image-guided IMRT—may substantially improve the results of this treatment. Backed by years of research, this technology integrates imaging and detection components into a state-of-the-art linear accelerator—allowing clinicians to both image and treat patients with a single device, so that the impact of motion can be reduced.

This leading-edge solution is generating a great amount of interest from the medical community, but its costs are even more overwhelming than before. Hospitals that want to acquire this technology are now faced with a similar challenge to that presented by Gamma Knife. American Shared can help them obtain this technology with a minimal investment—and without the risk of technological obsolescence.

With our creative financing models, strong presence in the radiation therapy market, and strategic alliances with the top tier of medical institutions, American Shared is in an excellent position to capitalize on this emerging market. We have focused our marketing efforts in this area, and anticipate increasing interest over the coming year.

AS THE LEADING PROVIDER OF GAMMA KNIFE SOLUTIONS, WE ARE STRONGLY POSITIONED FOR EXPANSION INTO THE NEW IMAGE-GUIDED IMRT MARKET.

BUILDING ON OUR TRACK RECORD—

THROUGH BREAKTHROUGH TECHNOLOGIES

NEW MARKETS

OR21 ... and more

BEYOND:

At American Shared, we're known for innovation. Our creative financing packages have made us a leader in our industry. Now, we're applying that same creativity to new and exciting ventures with the potential to further strengthen our growth:

- Our Operating Room for the 21st Century® (OR21®) concept is close to completion. OR21 will offer turnkey development of state-of-the-art surgical suites to major medical centers on a fee-per-use or other shared revenue basis. These suites will include the latest in operating room design, imaging capability, equipment integration, and patient monitoring. Operating rooms can be designed to accommodate multiple specialties or individualized to treat a special disease category. Specialties that can benefit from OR21 are cardiology, cardiac surgery, neurosurgery, neurology, vascular surgery, stroke therapy, spine surgery, orthopedics, and interventional radiology.
- Our proprietary tax-exempt financing concept enables non-profit institutions to make large capital acquisitions through tax-exempt operating leases, with the option to purchase or return the equipment at the end of the lease. In addition to providing financing for non-profit institutions, this unique tax-exempt financing program is also a potential financing vehicle for OR21.



OR21 COMBINES STATE-OF-THE-ART DESIGN AND EQUIPMENT WITH OUR PROVEN FINANCING MODELS – ALLOWING HOSPITALS TO OBTAIN ADVANCED SURGICAL TECHNOLOGIES WITH A MINIMAL INVESTMENT.

MOVING IN NEW DIRECTIONS—

THROUGH INNOVATIVE IDEAS AND PARTNERSHIPS

NEW TECHNOLOGIES

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American Shared Hospital Services

SELECTED FINANCIAL DATA

SUMMARY OF OPERATIONS

(Amounts in thousands except per share data) Year Ended December 31,	2004	2003	2002	2001	2000
Medical services revenue	\$16,389	\$16,178	\$13,366	\$11,758	\$ 9,336
Costs of operations	7,887	7,400	5,399	4,285	3,435
Selling and administrative expense	2,963	3,255	3,313	3,245	2,655
Interest expense	2,261	2,547	2,437	2,456	2,118
Total costs and expenses	13,111	13,202	11,149	9,986	8,208
Income from operations	3,278	2,976	2,217	1,772	1,128
Interest and other income	102	121	171	480	829
Minority interest	(983)	(928)	(831)	(751)	(645)
Income before income taxes	2,397	2,169	1,557	1,501	1,312
Income tax benefit (expense)	(412)	(787)	(455)	(433)	0
Net income	\$ 1,985	\$ 1,382	\$ 1,102	\$ 1,068	\$ 1,312
Net income per common share:					
Basic	\$ 0.46	\$ 0.36	\$ 0.30	\$ 0.30	\$ 0.34
Diluted	\$ 0.39	\$ 0.27	\$ 0.22	\$ 0.21	\$ 0.24
Cash dividend declared per common share	\$0.1725	\$0.2000	\$0.1200	\$0.1000	\$0.0000
Dividend payout ratio (paid and declared)	0.44	0.74	0.55	0.48	—
See accompanying note					

BALANCE SHEET DATA

(Amounts in thousands) Year Ended December 31,	2004	2003	2002	2001	2000
Cash & cash equivalents	\$ 8,121	\$10,312	\$ 9,924	\$11,580	\$12,421
Securities	957	0	0	0	0
Restricted cash	50	50	50	50	50
Working capital	4,717	5,268	7,175	9,351	10,155
Total assets	47,106	46,304	44,830	42,385	40,209
Current portion of long-term debt	6,562	6,803	5,490	4,305	4,126
Long-term debt, less current portion	18,924	20,114	22,006	21,615	20,300
Shareholders' equity	\$17,546	\$15,329	\$14,540	\$13,785	\$13,658

See accompanying note

(1) In October 1995, the Company entered into an operating agreement granting to American Shared Radiosurgery Services (a California corporation and a wholly-owned subsidiary of the Company) an 81% ownership interest in GK Financing, LLC ("GKF"). ASHS incorporated a new wholly-owned subsidiary, OR21, Inc. ("OR21") in November 1999, and a new wholly-owned subsidiary, MedLeader.com, Inc. ("MedLeader") in April 2000. Accordingly, the financial data for the Company presented above include the results of GKF, OR21 and MedLeader for 2000 through 2004.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

APPLICATION OF CRITICAL ACCOUNTING POLICIES

The Company's consolidated financial statements are prepared in accordance with generally accepted accounting principles and follow general practices within the industry in which it operates. Application of these principles requires management to make estimates, assumptions and judgments that affect the amounts reported in the financial statements and accompanying notes. These estimates, assumptions and judgments are based on information available as of the date of the financial statements; accordingly, as this information changes, the financial statements could reflect different estimates, assumptions and judgments. Certain policies inherently have a greater reliance on the use of estimates, assumptions and judgments and as such have a greater possibility of producing results that could be materially different than originally reported. Estimates, assumptions and judgments are necessary when assets and liabilities are required to be recorded at fair value, when a decline in the value of an asset not carried on the financial statements at fair value warrants an impairment write-down or valuation reserve to be established, or when an asset or liability needs to be recorded contingent upon a future event. Carrying assets and liabilities at fair value inherently results in more financial statement volatility. The fair values and the information used to record valuation adjustments for certain assets and liabilities are based either on quoted market prices or are provided by other third-party sources when available. When third-party information is not available, valuation adjustments are estimated in good faith by management primarily through the use of internal cash flow modeling techniques.

The most significant accounting policies followed by the Company are presented in Note 2 to the consolidated financial statements. These policies along with the disclosures presented in the other financial statement notes and in this financial review, provide information on how significant assets and liabilities are valued in the financial statements and how those values are determined. Based on the valuation techniques used and the sensitivity of financial statement amounts to the methods, assumptions and estimates underlying those amounts, management has identified the determination of the allowance for doubtful accounts and revenue recognition to be two areas that required the most subjective or complex judgments, and as such could be most subject to revision as new information becomes available. The following are our critical accounting policies in which management's estimates, assumptions and judgments most directly and materially affect the financial statements:

Revenue Recognition The Company has only one revenue-generating activity, which is the operation of Gamma Knife units by GK Financing, LLC ("GKF"), an 81% owned subsidiary of the Company.

Revenue is recognized when services have been rendered and collectibility is reasonably assured, on either a fee per use or revenue sharing basis. The Company has 14 fee per use hospitals and five retail hospitals. Under both of these types of agreements, the hospital is responsible for billing patients and collection of fees for services performed. Revenue associated with installation of the Gamma Knife units, if any, is a part of the negotiated lease amount and not a distinctly identifiable amount. The costs, if any, associated with installation of the units are amortized over the period of the related lease to match revenue recognition of these costs.

For fee per use agreements, revenue is not estimated because these contracts provide for a fixed fee per procedure, and are typically for a ten year term. Revenue is recognized at the time the procedures are performed, based on each hospital's contracted rate. There is no guaranteed minimum payment. Costs related to operating the units are charged to costs of operations as incurred, which approximates the recognition of the related revenue. Revenues under fee per use agreements are recorded on a gross basis.

GKF has five leases that are based on revenue sharing. These can be further classified as either "turn-key" arrangements or "net revenue sharing" arrangements. For the three turn-key sites, GKF is solely responsible for the costs to acquire and install the Gamma Knife. In return, GKF receives payment from the hospital in the amount of its reimbursement from third party payors. Revenue is recognized by the Company

during the period in which the procedure is performed, and is estimated based on what can be reasonably expected to be paid by the third party payor to the hospital. The estimate is primarily determined from historical experience and hospital contracts with third party payors. These estimates are reviewed on a regular basis and adjusted as necessary to more accurately reflect the expected payment amount. The Company also records an estimate of operating costs associated with each procedure during the period in which the procedure is performed. Costs are determined primarily based on historical treatment protocols and cost schedules with the hospital. The Company's estimated operating costs are reviewed on a regular basis and adjusted as necessary to more accurately reflect the actual operating costs. Revenue for turn-key sites is recorded on a gross basis, and the operating expenses the Company reimburses to the hospital are recorded in other operating costs.

Under net revenue sharing arrangements the hospital shares in the responsibility and risk with GKF for the capital investment to acquire and install the Gamma Knife. Unlike our turn-key arrangement, GKF's lease payment under a net revenue sharing arrangement is a percentage of revenue less operating costs. Payments are made by the hospital, generally on a monthly basis, to GKF based on an agreed upon percentage allocation of income remaining after all operating expenses are deducted from cash collected. Revenue is recognized during the period in which the procedure is performed, and is determined based on the net reimbursement amount that GKF expects to receive from the hospital for each Gamma Knife procedure. Under the net revenue sharing arrangement, the percent of revenue received by GKF is recorded net of costs to provide a Gamma Knife treatment. This estimate is reviewed on a regular basis and adjusted as necessary to more accurately reflect the expected payment amount.

Revenue from retail arrangements amounted to approximately 25%, 24% and 25% of revenue for the years ended December 31 2004, 2003 and 2002, respectively.

Allowance for Doubtful Accounts The allowance for doubtful accounts is estimated based on possible losses relating to the Company's revenue sharing customers. The Company receives reimbursement from the customer based on the customer's collections from individuals and third-party payors such as insurance companies and Medicare. Receivables are charged against the allowance in the period that they are deemed uncollectible.

If the Company's net accounts receivable estimates for revenue sharing customers as of December 31, 2004 changed by as much as 10% based on actual collection information, it would have the effect of increasing or decreasing revenue by approximately \$130,000.

GENERAL

During the years ended December 31, 2004, 2003 and 2002, 100% of the Company's revenue was derived from its Gamma Knife business.

TOTAL REVENUE

	2004	Increase (Decrease)	2003	Increase (Decrease)	2002
Medical services revenue (in thousands)	\$16,389	1.3%	\$16,178	21.0%	\$13,366
Number of Gamma Knife procedures	2,140	1.1%	2,116	24.8%	1,696
Average revenue per procedure	\$ 7,658	0.2%	\$ 7,646	(3.0)%	\$ 7,881

Medical services revenue increased 1.3% in 2004 compared to 2003 and increased 21.0% in 2003 compared to 2002. The increase in 2004 is due to an increase in the number of Gamma Knife units in operation. The increase in 2003 is attributable to an increase in revenue at locations in operation for more than one year, as well as an increase in the number of Gamma Knife units in operation.

Gamma Knife revenue increased \$211,000 and \$2,812,000 in 2004 and 2003, respectively, compared to the prior years. The 2004 increase was due to one new Gamma Knife unit that began operation during 2004 and the full year inclusion of three new Gamma Knife units that began operation during 2003, which offset a 14% decrease in revenue for Gamma Knife units in operation more than one year. The 2003 increase was primarily due to three new Gamma Knife units that began operation during 2003, the full year inclusion of two Gamma Knife units that began operation during 2002, and a 5% increase in revenue for Gamma Knife units in operation more than one year. The Company had eighteen, seventeen and fourteen Gamma Knife units in operation at December 31, 2004, 2003 and 2002, respectively.

The increase in the number of Gamma Knife procedures in 2004 compared to 2003 was due to the increase in the number of Gamma Knife units in operation, which offset a 10% decrease in procedures for Gamma Knife units in operation more than one year. The number of Gamma Knife procedures in 2003 increased by 420 compared to 2002 due to the increase in the number of Gamma Knife units in operation, as well as a 9% increase in procedures for Gamma Knife units in operation more than one year.

Revenue per procedure increased \$12 in 2004 compared to 2003. The Company's contracts generally have different procedure rates because their investment basis varies, so revenue per procedure can vary year to year depending primarily on the mix of procedures performed at certain locations. Gamma Knife revenue per procedure decreased by \$235 in 2003 compared to 2002 primarily because there was an increase in the number of procedures performed at certain Gamma Knife locations that have a lower per procedure rate, as well as a decrease in the amounts received from Medicare at one of the Company's retail sites.

COSTS OF OPERATIONS

(In thousands)	2004	Increase	2003	Increase	2002
Costs of operations	\$7,887	6.6%	\$7,400	37.1%	\$5,399
Percentage of revenue	48.1%		45.7%		40.4%

The Company's costs of operations, consisting of maintenance and supplies, depreciation and amortization, and other operating expenses (such as insurance, property taxes, sales taxes, marketing costs and other fees) increased \$487,000 in 2004 compared to 2003, and increased \$2,001,000 in 2003 compared to 2002.

The Company's maintenance and supplies costs were 5%, 5% and 3% of medical service revenue in 2004, 2003 and 2002, respectively. Maintenance and supplies costs increased \$139,000 in 2004 compared to 2003, and increased \$301,000 in 2003 compared to 2002. The increase in 2004 compared to 2003 was primarily due to the expiration of the warranty period on two Gamma Knife units and the full year inclusion of three Gamma Knife units whose warranty period expired during 2003. The increase in 2003 compared to 2002 was primarily due to the expiration of the warranty period on three Gamma Knife units and the full year inclusion of maintenance on two Gamma Knife units whose warranty period expired during the previous year.

Depreciation and amortization increased \$577,000 in 2004 compared to 2003, and increased \$753,000 in 2003 compared to 2002. The increase in 2004 was due to the addition of one new Gamma Knife unit that commenced operation during third quarter 2004 and a full year's depreciation on three Gamma Knife units that started operation in 2003. The increase in 2003 was due to the addition of three new Gamma Knife units that commenced operation during first, second and third quarters of 2003 and a full year of depreciation on two new Gamma Knife units that started operation during 2002.

Other direct operating costs as a percentage of medical services revenue were 13%, 15% and 11% in 2004, 2003 and 2002, respectively. The decrease of \$229,000 in 2004 compared to 2003 was primarily due to lower operating costs related to a lower number of procedures performed at one of the Company's retail locations. The increase of \$947,000 in 2003 compared to 2002 was primarily due to increased spending for marketing, increased operating costs related to the Company's additional retail units, startup and training costs at the Company's three new Gamma Knife centers, and higher insurance and taxes due to additional Gamma Knife units in operation.

SELLING AND ADMINISTRATIVE

(In thousands)	2004	Increase (Decrease)	2003	Increase (Decrease)	2002
Selling and administrative costs	\$2,963	(9.0)%	\$3,255	(1.8)%	\$3,313
Percentage of revenue	18.1%		20.1%		24.8%

The Company's selling and administrative costs decreased \$292,000 in 2004 compared to 2003, and decreased \$58,000 in 2003 compared to 2002. The decrease in 2004 was primarily due to lower payroll and business development costs of approximately \$142,000, recruiting fees of \$42,000 and insurance of \$26,000. Also, during 2003 there was a non-recurring write-off of approximately \$58,000 in previously deferred costs relating to the future placement of a Gamma Knife unit in Brazil, and the Company's Gamma Knife User's Meeting of approximately \$45,000. The decrease in 2003 from 2002 was primarily due to reduced business development costs of approximately \$152,000 and legal and accounting fees of \$104,000. These reductions were partially offset by increased employment recruiting fees of \$60,000, the Company's Gamma Knife User's Meeting of approximately \$45,000 and a write-off of approximately \$58,000 in previously deferred costs relating to the future placement of a Gamma Knife unit in Brazil, which was reallocated to another location.

INTEREST EXPENSE

(In thousands)	2004	Increase (Decrease)	2003	Increase (Decrease)	2002
Interest expense	\$2,261	(11.2)%	\$2,547	4.5%	\$2,437
Percentage of revenue	13.8%		15.7%		18.2%

The Company's interest expense decreased \$286,000 in 2004 compared to 2003, and increased \$110,000 in 2003 compared to 2002. The decrease in 2004 was primarily due to lower interest expense on the Company's more mature Gamma Knife units and final payment on the debt for one Gamma Knife unit. This decrease was partially offset by additional interest expense on the financing of the Company's new Gamma Knife unit in 2004. The increase in 2003 was due to additional interest expense on the financing of the Company's three new Gamma Knife units in 2003, which was partially offset by lower interest expense on the Company's more mature Gamma Knife units. Except for one unit that has been paid in full, all of the Company's operating Gamma Knife units are financed by means of interest bearing debt. Twelve of the Company's eighteen Gamma Knife units have been in operation for more than three years, and have lower interest expense than newer units because interest expense decreases with each principal payment.

OTHER INCOME AND EXPENSE

(In thousands)	2004	Increase (Decrease)	2003	Increase (Decrease)	2002
Interest and other income	\$ 102	(15.7)%	\$ 121	(29.2)%	\$ 171
Percentage of revenue	0.6%		0.7%		1.3%
Minority interest expense	\$(983)	5.9%	\$(928)	11.7%	\$(831)
Percentage of revenue	(6.0)%		(5.7)%		(6.2)%

Interest and other income decreased \$19,000 in 2004 compared to 2003 and decreased \$50,000 in 2003 compared to 2002. The decrease in 2004 was primarily due to lower invested cash balances during 2004. The decrease in 2003 was primarily due to lower invested cash balances during 2003 and lower interest rates during 2003 compared to 2002.

Minority interest increased \$55,000 in 2004 and \$97,000 in 2003 compared to the prior year, respectively. Minority interest represents the pre-tax income earned by the minority partner's 19% interest in GKF. The increase in minority interest reflects the increased profitability of GKF.

INCOME TAXES

(In thousands)	2004	Increase (Decrease)	2003	Increase (Decrease)	2002
Income tax benefit (expense)	\$(412)	(47.6%)	\$(787)	73.0%	\$(455)
Percentage of revenue	2.5%		4.9%		3.4%

Income tax expense decreased \$375,000 in 2004 compared to 2003, and increased \$332,000 in 2003 compared to 2002. The Company's 40% income tax provision for 2004 was reduced by a \$547,000 income tax benefit from the exercise of options to purchase 846,000 common shares. The Company's 40% income tax provision for 2003 was reduced by an \$81,000 income tax benefit from the exercise of options to purchase 125,000 common shares. The income tax benefit is a result of compensation expense that was recognized when these options for common shares were granted in 1995.

The Company anticipates that it will continue to record income tax expense if it operates profitably in the future. Currently there are minimal income tax payments required due to net operating loss carryforwards and other deferred tax assets available for tax purposes.

The Company had a net operating loss carryforward for federal income tax return purposes at December 31, 2004 of approximately \$12,000,000.

NET INCOME

(In thousands) except per share amounts)	2004	Increase (Decrease)	2003	Increase (Decrease)	2002
Net income	\$1,985	43.6%	\$1,382	25.4%	\$1,102
Net income per share	\$ 0.46	27.8%	\$ 0.36	20.0%	\$ 0.30

The Company had net income of \$1,985,000 in 2004 compared to \$1,382,000 in 2003 and \$1,102,000 in 2002. Net income for 2004 included increased income from operations compared to 2003 of \$302,000 which was primarily due to lower selling and administrative costs and interest expense. In addition, income tax expense was \$375,000 less than 2003 due to an income tax benefit of \$547,000 on the exercise of options to purchase common stock. Net income for 2003 included increased income from operations of \$759,000 compared to 2002, which was primarily due to the addition of three new Gamma Knife units and a 5% increase in revenue from Gamma Knife units in operation more than one year.

LIQUIDITY AND CAPITAL RESOURCES

The Company had cash and cash equivalents of \$8,121,000 at December 31, 2004 compared to \$10,312,000 at December 31, 2003. The Company's expected primary cash needs on both a short and long-term basis are for capital expenditures, business expansion, working capital, payment of quarterly dividends and other general corporate purposes.

Securities of \$957,000 represents a portion of the Company's cash that is invested in high-quality short to intermediate-term fixed income securities in order to maximize income on its available cash. It is the Company's intent to hold these securities until maturity.

Restricted cash of \$50,000 at December 31, 2004 reflects cash that may only be used for the operations of GKF.

Operating activities provided cash of \$7,608,000 in 2004. Net income of \$1,985,000, depreciation and amortization of \$4,892,000 and an increase in the minority interest of \$983,000 were the primary reasons. The Company's trade accounts receivable increased to \$2,793,000 at December 31, 2004 from \$2,209,000 at December 31, 2003. This increase was primarily due to the addition of one new Gamma Knife contract during 2004 and an increase in the number of days revenue outstanding ("DSO") in accounts receivable for some of the Gamma Knife contracts. The DSO was 66 and 54 days as of December 31, 2004 and December 31, 2003, respectively. We expect DSO to fluctuate in the future depending on timing of customer payments received and the mix of fee per use vs. retail customers. Other receivables decreased by \$101,000 primarily due to application of credits due on certain under-funded loans.

Investing activities used \$1,325,000 of cash in 2004 primarily due to an investment in short to mid-term securities of \$957,000 and for the purchase of site improvements at certain Gamma Knife locations.

Financing activities used \$8,474,000 of cash during 2004, primarily due to principal payments on long-term debt of \$7,371,000, distributions to minority owners of \$399,000 and the payment of dividends of \$699,000.

Working capital decreased \$551,000 to \$4,717,000 at December 31, 2004 from \$5,268,000 at December 31, 2003 primarily due to a decrease in cash and securities of \$1,234,000 which was partially offset by an increase in trade accounts receivable of \$584,000.

The Company primarily invests its cash in money market or similar funds and high quality short to mid-term securities in order to minimize the potential for principal erosion. Cash is invested in these short-term funds pending use in the Company's operations. The Company believes its cash position combined with its working capital is adequate to service the Company's cash requirements in 2005.

The Company finances all of its Gamma Knife units, and anticipates that it will continue to do so with future contracts, but there can be no assurance that financing will continue to be available on acceptable terms. During 2003 the Company's primary lender, DVI, filed for Chapter 11 bankruptcy protection. The Company made claims in DVI's bankruptcy case for certain unfunded amounts under credit agreements in place at the time of the bankruptcy filing. The principal balance of notes that included the unfunded amounts were transferred by DVI to a third party lender, and the Company has subsequently satisfactorily resolved any issues related to these unfunded amounts with that lender. The Company continues to make payments on the outstanding note balances serviced by the third party lender who acts as successor servicer. The Company has secured financing for its current projects in progress and anticipates that it will be able to secure financing on future projects from other lending sources on comparable terms. The Company meets all debt covenants required under notes with its lenders, and expects that any covenants required by future lenders will be acceptable to the Company.

IMPACT OF INFLATION AND CHANGING PRICES

The Company does not believe that inflation has had a significant impact on operations because a substantial majority of the costs that it incurs under its customer contracts are fixed through the term of the contract.

CONTRACTUAL OBLIGATIONS, COMMITMENTS, CONTINGENT LIABILITIES AND OFF BALANCE SHEET ARRANGEMENTS

The following table presents, as of December 31, 2004, the Corporation's significant fixed and determinable contractual obligations by payment date. The payment amounts represent those amounts contractually due to the recipient and do not include any unamortized premiums or discounts, hedge basis adjustments, or other similar carrying value adjustments. Further discussion of the nature of each obligation is included in the referenced note to the consolidated financial statements.

Contractual Obligations	Payments Due by Period				
	Total amounts committed	Less than 1 year	1-3 years	4-5 years	After 5 years
Long-term debt	\$25,486,000	\$6,562,000	\$16,024,000	\$2,900,000	
Future Gamma Knife purchases ⁽¹⁾	3,840,000		3,840,000		
Operating leases	502,000	303,000	199,000		
Total contractual obligations	\$29,828,000	\$6,865,000	\$20,063,000	\$2,900,000	\$0

(1) The Company has deposits toward the purchase of future Gamma Knife units as more fully described in Note 10 of the consolidated financial statements. It is uncertain when these units will be placed in service, so it cannot be determined when the commitment is due. For purposes of this table, these commitments are listed in the 1-3 year category.

Further discussion of the long-term debt commitment is included in Note 4, and operating leases in Note 9 of the consolidated financial statements.

The Company has no significant off-balance sheet arrangements.

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The table below presents information about certain market-sensitive financial instruments as of December 31, 2004. The fair values were determined based on quoted market prices for the same or similar instruments.

We do not hold or issue derivative instruments for trading purposes and are not a party to any instruments with leverage or prepayment features.

(amounts in thousands)	Maturity Date, Year ending December 31						Total	Fair Value
	2005	2006	2007	2008	2009	Thereafter		
Fixed-rate long-term debt	\$6,562	\$9,533	\$3,773	\$2,718	\$2,625	\$275	\$25,486	\$25,637
Average interest rates	9.1%	8.9%	8.8%	8.5%	8.3%	8.4%	8.9%	

At December 31, 2004, we had no significant long-term, market-sensitive investments. Our cash is invested primarily in short-term money market or similar funds to minimize potential for principal erosion.

We have no affiliation with partnerships, trust or other entities whose purpose is to facilitate off-balance sheet financial transactions or similar arrangements, and therefore have no exposure to the financing, liquidity, market or credit risks associated with such entities.

American Shared Hospital Services

CONSOLIDATED BALANCE SHEETS

December 31,	2004	2003
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$ 8,121,000	\$10,312,000
Securities	957,000	—
Restricted cash	50,000	50,000
Trade accounts receivable, net of allowance for doubtful accounts of \$170,000 in 2004 and \$170,000 in 2003	2,793,000	2,209,000
Other receivables	157,000	258,000
Prepaid expenses and other current assets	594,000	473,000
Total current assets	12,672,000	13,302,000
PROPERTY AND EQUIPMENT, net	34,272,000	32,828,000
OTHER ASSETS	162,000	174,000
	\$47,106,000	\$46,304,000
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES		
Accounts payable	\$ 282,000	\$ 371,000
Accrued interest and other liabilities	1,023,000	734,000
Employee compensation and benefits	88,000	126,000
Current portion of long-term debt	6,562,000	6,803,000
Total current liabilities	7,955,000	8,034,000
LONG-TERM DEBT, less current portion	18,924,000	20,114,000
DEFERRED INCOME TAXES	366,000	1,096,000
MINORITY INTEREST	2,315,000	1,731,000
SHAREHOLDERS' EQUITY		
Common stock, no par value		
Authorized—10,000,000 shares		
Issued and outstanding shares—4,776,000 in 2004 and 3,918,000 in 2003	9,238,000	9,198,000
Additional paid-in capital	4,410,000	3,461,000
Retained earnings	3,898,000	2,670,000
Total shareholders' equity	17,546,000	15,329,000
	\$47,106,000	\$46,304,000

See accompanying notes

American Shared Hospital Services

CONSOLIDATED STATEMENTS OF OPERATIONS

Years Ended December 31,	2004	2003	2002
REVENUE:			
Medical services	\$16,389,000	\$16,178,000	\$13,366,000
COSTS AND EXPENSES:			
Costs of operations:			
Maintenance and supplies	885,000	746,000	445,000
Depreciation	4,802,000	4,225,000	3,472,000
Other direct operating costs	2,200,000	2,429,000	1,482,000
Selling and administrative	2,963,000	3,255,000	3,313,000
Interest	2,261,000	2,547,000	2,437,000
Total costs and expenses	13,111,000	13,202,000	11,149,000
Operating income	3,278,000	2,976,000	2,217,000
Interest and other income	102,000	121,000	171,000
Minority interest expense	(983,000)	(928,000)	(831,000)
Income before income taxes	2,397,000	2,169,000	1,557,000
Income tax expense	(412,000)	(787,000)	(455,000)
NET INCOME	\$ 1,985,000	\$ 1,382,000	\$ 1,102,000
Earnings per common share—basic	\$0.46	\$0.36	\$0.30
Earnings per common share—diluted	\$0.39	\$0.27	\$0.22

See accompanying notes

CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY

Three Years Ended December 31, 2004	Common Shares	Common Stock	Additional Paid-in Capital	Retained Earnings	Total
Balances at January 1, 2002	3,525,000	\$9,240,000	\$3,154,000	\$1,391,000	\$13,785,000
Options exercised	300,000	68,000	158,000	—	226,000
Repurchase of common stock and options	(42,000)	(135,000)	—	—	(135,000)
Dividends	—	—	—	(438,000)	(438,000)
Net income	—	—	—	1,102,000	1,102,000
Balances at December 31, 2002	3,783,000	9,173,000	3,312,000	2,055,000	14,540,000
Options exercised	135,000	25,000	163,000	—	188,000
Repurchase of common stock and options	—	—	(14,000)	—	(14,000)
Dividends	—	—	—	(767,000)	(767,000)
Net income	—	—	—	1,382,000	1,382,000
Balances at December 31, 2003	3,918,000	9,198,000	3,461,000	2,670,000	15,329,000
Options exercised	858,000	40,000	994,000	—	1,034,000
Repurchase of stock options	—	—	(45,000)	—	(45,000)
Dividends	—	—	—	(757,000)	(757,000)
Net income	—	—	—	1,985,000	1,985,000
Balances at December 31, 2004	4,776,000	\$9,238,000	\$4,410,000	\$3,898,000	\$17,546,000

See accompanying notes

American Shared Hospital Services

CONSOLIDATED STATEMENTS OF CASH FLOWS

Years Ended December 31,	2004	2003	2002
OPERATING ACTIVITIES			
Net income	\$ 1,985,000	\$ 1,382,000	\$ 1,102,000
Adjustments to reconcile net income to net cash from operating activities:			
Gain on sale of assets, early termination of capital leases	—	—	3,000
Depreciation and amortization	4,892,000	4,313,000	3,529,000
Deferred income tax liability	264,000	669,000	365,000
Minority interest in consolidated subsidiaries	983,000	928,000	831,000
Changes in operating assets and liabilities:			
Receivables	(483,000)	104,000	(202,000)
Prepaid expenses and other assets	(137,000)	426,000	(75,000)
Accounts payable and accrued liabilities	104,000	318,000	(376,000)
Net cash from operating activities	7,608,000	8,140,000	5,177,000
INVESTING ACTIVITIES			
Payment for purchase of property and equipment	(368,000)	(731,000)	(1,346,000)
Investment in securities	(957,000)	—	—
Net cash from investing activities	(1,325,000)	(731,000)	(1,346,000)
FINANCING ACTIVITIES			
Principal payments on long-term debt and obligations under capital leases	(7,371,000)	(5,777,000)	(4,434,000)
Payment of dividends	(699,000)	(610,000)	(438,000)
Distributions to minority owners	(399,000)	(645,000)	(548,000)
Proceeds from exercise of stock warrants and options	40,000	25,000	68,000
Repurchase of stock options/warrants	(45,000)	(14,000)	—
Repurchase of common stock	—	—	(135,000)
Net cash from financing activities	(8,474,000)	(7,021,000)	(5,487,000)
Net increase (decrease) in cash and cash equivalents	(2,191,000)	388,000	(1,656,000)
CASH AND CASH EQUIVALENTS, beginning of year	10,312,000	9,924,000	11,580,000
CASH AND CASH EQUIVALENTS, end of year	\$ 8,121,000	\$10,312,000	\$ 9,924,000
SUPPLEMENTAL CASH FLOW DISCLOSURE			
Interest paid	\$ 2,500,000	\$ 2,692,000	\$ 2,428,000
Income taxes paid	\$ 129,000	\$ 88,000	\$ 90,000
SCHEDULE OF NONCASH INVESTING AND FINANCING ACTIVITIES			
Acquisition of equipment with lease/debt financing	\$ 5,940,000	\$ 5,198,000	\$ 6,010,000
Accrued dividends	\$ 215,000	\$ 157,000	\$ —
Income tax benefit from stock option exercise recorded to Additional paid-in capital	\$ 994,000	\$ 163,000	\$ 158,000

See accompanying notes

NOTE 1—BUSINESS AND BASIS OF PRESENTATION

Business American Shared Hospital Services (the “Company”), a California corporation, provides Leksell Gamma Knife® (“Gamma Knife”) units to eighteen medical centers in Arkansas, California, Connecticut, Florida, Illinois, Maryland, Massachusetts, Mississippi, Nevada, New Jersey, New Mexico, New York, Ohio, Pennsylvania, Texas and Wisconsin.

The Company (through American Shared Radiosurgery Services (“ASRS”)) and Elekta AB, the manufacturer of the Gamma Knife (through its wholly owned United States subsidiary GKV Investments, Inc. (“GKV”)), entered into an operating agreement and formed GK Financing, LLC (“GKF”). GKF provides alternative financing of Gamma Knife units and is the preferred provider for Elekta AB of financing arrangements, such as fee-for-service lease arrangements with health care institutions.

OR21, Inc., is a wholly-owned subsidiary of the Company that will provide the product “The Operating Room for the 21st Century®”, which is currently under development.

MedLeader.com, Inc., is a wholly-owned subsidiary of the Company that will provide continuing medical education online and through videos for doctors, nurses and other healthcare workers. This subsidiary is not operational at this time.

The consolidated financial statements include the accounts of the Company, its wholly owned subsidiaries, OR21, Inc., MedLeader.com, Inc., ASRS and its majority-owned subsidiary, GK Financing, LLC.

All significant intercompany accounts and transactions have been eliminated in consolidation.

NOTE 2—ACCOUNTING POLICIES

Use of estimates in the preparation of financial statements In preparing financial statements in conformity with generally accepted accounting principles, management makes estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements, as well as the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and cash equivalents The Company considers all liquid investments with original maturities of three months or less at the date of purchase to be cash equivalents. Restricted cash is not considered a cash equivalent for purposes of the consolidated statements of cash flows.

Securities The Company invests excess cash in short to intermediate term fixed income securities. It is the Company’s intent and ability to hold these securities until maturity and they are therefore regarded as *held-to-maturity* investments. As of December 31, 2004, the cost of these securities approximated fair market value, and they ranged in maturity up to six months.

Restricted cash Restricted cash represents the minimum cash that, by agreement, must be maintained in GK Financing, LLC to fund operations.

Business and credit risk The Company maintains its cash balances in financial institutions which exceed federally insured limits, and the Company’s securities are invested in short to intermediate term fixed income

securities that are not insured. The Company has not experienced any losses and believes it is not exposed to any significant credit risk on cash, cash equivalents and securities.

All of the Company's revenue is provided by eighteen customers. These customers constitute accounts receivable at December 31, 2004. The Company performs credit evaluations of its customers and generally does not require collateral. The Company has not experienced significant losses related to receivables from individual customers or groups of customers in any particular industry or geographic area.

Accounts receivable and doubtful accounts Accounts receivable are recorded at net realizable value. An allowance for doubtful accounts is estimated based on historical collections plus an allowance for probable losses. Receivables are considered past due based on contractual terms and are charged off in the period that they are deemed uncollectible. Recoveries of receivables previously charged off are recorded when received.

Accounting for majority-owned subsidiary The Company accounts for GKF as a consolidated entity due to its 81% majority-equity interest.

Property and equipment Property and equipment are stated at cost less accumulated depreciation. Depreciation is determined using the straight-line method over the estimated useful lives of the assets, which for medical and office equipment is generally 3–15 years. The Company capitalized interest of \$94,000 and \$202,000 in 2004 and 2003, respectively, as costs of medical equipment.

The Company leases Gamma Knife equipment to its customers under arrangements accounted for as operating leases. At December 31, 2004, the Company held equipment under operating lease contracts with customers with an original cost of \$46,915,000 and accumulated depreciation of \$19,010,000. At December 31, 2003, the Company held equipment under operating lease contracts with customers with an original cost of \$43,710,000 and accumulated depreciation of \$14,455,000.

Revenue recognition Revenue is recognized when services have been rendered and collectibility is reasonably assured. There are no guaranteed minimum payments. The Company's contracts are typically for a ten year term and are classified as either fee per use or retail. Retail arrangements are further classified as either turn-key or net revenue sharing. Revenue from fee per use contracts is recorded on a gross basis as determined by each hospital's contracted rate. Under turn-key arrangements, the Company receives payment from the hospital in the amount of its reimbursement from third party payors, and is responsible for paying all the operating costs of the Gamma Knife. Revenue is recorded on a gross basis and estimated based on historical experience and hospital contracts with third party payors. For net revenue sharing arrangements the Company receives a contracted percentage of the reimbursement received by the hospital less the operating expenses of the Gamma Knife. Revenue is recorded on a net basis and estimated based on historical experience. Any revenue estimates are reviewed periodically and adjusted as necessary. Revenue recognition is consistent with guidelines provided under EITF 99-19.

Income taxes The Company accounts for income taxes in accordance with SFAS No 109, *Accounting for Income Taxes*. Under this method, deferred tax assets and liabilities are determined based on differences between the financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse.

Earnings per share Basic earnings per share excludes dilution and is computed by dividing income available to common shareholders by the weighted average number of common shares outstanding for the year. Diluted earnings per share reflect the potential dilution that could occur if common shares were issued

pursuant to the exercise of options or warrants. The following table illustrates the computations of basic and diluted earnings per share for the years ended December 31, 2004, 2003 and 2002.

	2004	2003	2002
Numerator for basic and diluted earnings per share	\$1,985,000	\$1,382,000	\$1,102,000
Denominator:			
Denominator for basic earnings per share— weighted-average shares	4,351,000	3,850,000	3,707,000
Effect of dilutive securities Employee stock options/warrants	750,000	1,238,000	1,324,000
Denominator for diluted earnings per share— adjusted weighted-average shares	\$5,101,000	\$5,088,000	\$5,031,000
Earning per share—basic	\$ 0.46	\$ 0.36	\$ 0.30
Earning per share—diluted	\$ 0.39	\$ 0.27	\$ 0.22

In 2004 options outstanding to purchase 16,500 shares of common stock at an exercise price of \$5.50 per share were not included in the calculation of diluted earnings per share as the exercise price of the options was greater than the average market price of common stock during the year.

In 2002, options outstanding to purchase 17,500 shares of common stock at \$4.10 per share were not included in the computation of diluted earnings per share as the exercise price of the options was greater than the average market price of the common stock during the year.

Reclassifications Certain reclassifications have been made to the 2003 balances to conform with the 2004 presentation.

Stock-based compensation The Company has three stock-based employee compensation plans, which are described more fully in Note 7. The Company accounts for those plans under the recognition and measurement principles of APB Opinion No. 25, *Accounting for Stock Issued to Employees*, and related Interpretations. No stock-based employee compensation cost is reflected in net income, as all options granted under those plans had an exercise price greater than or equal to the market value of the underlying common stock on the date of grant. The following table illustrates the effect on net income and earnings per share if the Company had applied the fair value recognition provisions of FASB Statement No. 123, *Accounting for Stock-Based Compensation*, to stock-based employee compensation. For pro forma purposes, the estimated fair value of the Company's options is amortized over the options' vesting period, which is generally from one to five years.

Years Ended December 31,	2004	2003	2002
Net income, as reported	\$1,985,000	\$1,382,000	\$1,102,000
Deduct: total stock-based employee compensation expense determined under fair value based method for all awards (Note 7), net of related tax effects	(9,000)	(3,000)	(36,000)
Proforma net income	\$1,976,000	\$1,379,000	\$1,066,000
Earnings per share:			
Basic—as reported	\$ 0.46	\$ 0.36	\$ 0.30
Basic—pro forma	\$ 0.45	\$ 0.36	\$ 0.29
Diluted—as reported	\$ 0.39	\$ 0.27	\$ 0.22
Diluted—pro forma	\$ 0.39	\$ 0.27	\$ 0.21

Fair value of financial instruments The carrying amounts of financial instruments, including cash and cash equivalents, securities, restricted cash, accounts receivable, accounts payable, and other accrued liabilities approximated their fair value as of December 31, 2004 and 2003, because of the relatively short maturity of these instruments. The fair value of the Company's various debt obligations, discounted at currently available interest rates was approximately \$25,637,000 and \$27,366,000 at December 31, 2004 and 2003, respectively.

Business segment information The Company, which engages in the business of leasing equipment to health care providers, has one reportable segment, the Gamma Knife that non-invasively treats malignant and benign brain tumors, vascular malformations and trigeminal neuralgia.

Recent accounting pronouncements In December 2003, the FASB issued FIN 46(R): *Consolidation of Variable Interest Entities, an interpretation of ARB No. 51*, which replaces FASB Interpretation No. 46, *Consolidation of Variable Interest Entities* (VIE). This Interpretation addresses consolidation by business enterprises of Variable Interest Entities. It defines a VIE as a corporation, partnership, trust, or any other legal structure used for the business purpose that either: a) the equity investment is not sufficient to allow the entity to finance its activities without additional financial support, b) the equity investors lack one or more of the following: 1. the ability to make decisions; 2. the obligation to absorb expected losses of the entity; or 3. the right to receive any returns of the entity, and, c) the equity investors have voting rights disproportionate to their economic interest, and the activities of the entity are conducted on behalf of an investor with a disproportionately small voting interest. This interpretation requires that existing unconsolidated VIE's be consolidated by their primary beneficiaries. The Company does not have any VIE entities and accordingly the implementation of the Interpretation did not result in an impact on its financial statements.

In December 2004, the FASB issued Statement No. 123R, *Share-Based Payment*. This statement replaces FASB Statement No. 123, *Accounting for Stock-Based Compensation*, and supersedes APB Opinion No. 25, *Accounting for Stock Issued to Employees*. This statement amends FASB Statement No. 95, *Statement of Cash Flows*. This statement requires that the cost resulting from all share-based payment transactions be recognized in the financial statements. This statement requires that excess tax benefits be reported as a financing cash inflow rather than as a reduction of taxes paid. This Statement establishes fair value as the measurement objective in accounting for the cost of share-based payment arrangements and requires all entities to apply a fair-value-based measurement method in accounting for share-based payment transactions with employees. This cost will be recognized over the period during which an employee is required to provide service in exchange for the award—the requisite service period (usually the vesting period). The Company is required to adopt FASB Statement No. 123R in third quarter 2005. Based on the Company's historical stock option awards, adoption of this statement will have minimal impact on the Company's financial statements.

NOTE 3—PROPERTY AND EQUIPMENT

Property and equipment consists of the following:

December 31,	2004	2003
Medical equipment and facilities	\$ 49,336,000	\$ 46,126,000
Office equipment	438,000	376,000
Deposits and construction in progress	4,499,000	1,463,000
	54,273,000	47,965,000
Accumulated depreciation	(20,001,000)	(15,137,000)
Net property and equipment	\$ 34,272,000	\$ 32,828,000

NOTE 4—LONG-TERM DEBT

Long-term debt consists primarily of 23 notes with financing companies, related to Gamma Knife construction and installation, totaling \$25,486,000. These notes accrue interest at fixed annual rates between 8.05% and 10.95%, are payable in 60 to 84 monthly installments, mature between April 2005 and March 2010, and are collateralized by the respective Gamma Knife units. As of December 31, 2004 and December 31, 2003 the Company was in compliance with all debt covenants required under notes with its lenders. The following are contractual maturities of long-term debt by year at December 31, 2004:

Year ending December 31,	
2005	\$ 6,562,000
2006	9,533,000
2007	3,773,000
2008	2,718,000
2009	2,625,000
Thereafter	275,000
	\$25,486,000

The Company's primary lender, DVI Financial Services, Inc. (DVI), filed for Chapter 11 bankruptcy protection in August 2003, and all outstanding notes were assumed by another lender as successor servicer. The Company continues to make payments to the successor servicer on the outstanding note balances with DVI. The Company has secured financing for its current projects in progress and anticipates that it will be able to secure financing for those and future projects from these or other potential lending sources under comparable terms. Management believes that the financial condition of DVI will not have a material adverse effect on the Company's financial position or results of operations.

NOTE 5—INCOME TAXES

Significant components of the Company's deferred tax liabilities and assets as of December 31 are as follows:

December 31,	2004	2003
Deferred tax liabilities:		
Fixed assets	\$(5,548,000)	\$(5,420,000)
Total deferred tax liabilities	(5,548,000)	(5,420,000)
Deferred tax assets:		
Net operating loss carryforwards	4,418,000	3,806,000
Accrued reserves	263,000	90,000
Other—net	501,000	428,000
Total deferred tax assets	5,182,000	4,324,000
Net deferred tax liabilities	\$ (366,000)	\$(1,096,000)

The 2004 and 2003 tax provision reflects the deduction for tax purposes of non-qualified stock options exercised by the Company's Chairman and Chief Executive Officer. The benefit of the tax deduction is reflected as a direct increase to equity and an increase in the deferred tax asset of \$1,540,000 and \$244,000 for 2004 and 2003 respectively, which is described more fully in Note 7.

The components of the provision for income taxes consist of the following:

Years Ended December 31,	2004	2003	2002
Current:			
State	\$ 47,000	\$ 38,000	\$ 90,000
Deferred:			
Federal	296,000	649,000	282,000
State	69,000	100,000	83,000
	\$412,000	\$787,000	\$455,000

The provision for income taxes differs from the amount computed by applying the U.S. federal statutory tax rate (34% in 2004, 2003 and 2002) to income before taxes as follows:

Years Ended December 31,	2004	2003	2002
Computed expected tax	\$815,000	\$741,000	\$529,000
State income taxes, net of federal benefit	144,000	127,000	91,000
Stock options	(547,000)	(81,000)	(167,000)
Other	—	—	2,000
	\$412,000	\$787,000	\$455,000

At December 31, 2004, the Company had a net operating loss carryforward for federal income tax return purposes of approximately \$12,000,000 which expire between 2005 and 2024. A substantial part of this carryforward is subject to separate return limitations. The Company's ability to utilize its net operating loss carryforwards and other deferred tax assets may be limited in the event of a 50% or more ownership change within any three-year period. Future federal net operating losses generated by the Company can be carried forward for 20 years.

NOTE 6—MINORITY INTEREST

The Minority interest liability reflects the 19% interest by the minority partner in the Company's GK Financing, LLC subsidiary. The balance increases (decreases) by the minority partner's share of the earnings (losses) in GK Financing, LLC, and is reduced by any cash distributions made to the minority partner, per the following table:

Years Ended December 31,	2004	2003	2002
Beginning balance	\$1,731,000	\$1,448,000	\$1,165,000
Minority interest in GKF net income	983,000	928,000	831,000
Less: cash distributions	(399,000)	(645,000)	(548,000)
Minority interest	\$2,315,000	\$1,731,000	\$1,448,000

NOTE 7—SHAREHOLDERS' EQUITY

1984 Stock Option Plan Under the Company's 1984 Stock Option Plan (the "Plan"), as amended, a total of 475,000 stock options were authorized for grant. The Plan terminated according to its terms on March 1, 1994. Options granted pursuant to the Plan generally had lives of 10 years from the date of grant, subject to earlier

expiration in certain cases, such as termination of the grantee's employment. All outstanding options under this Plan were exercised in 2002.

1995 Stock Option Plan The Company's 1995 Stock Option Plan provides for nonqualified stock options and "incentive stock options." Under the 1995 Plan, 330,000 common shares are reserved for awards to officers and other key employees, non-employee directors, and advisors. Provisions of the 1995 Stock Option Plan include an automatic grant to each non-employee director of options to purchase up to 4,000 shares annually on the date of the Company's Annual Shareholder Meeting, at an exercise price equal to the market price of the Company's common shares on that date, until the non-employee director has options for a total of 12,000 shares of the Company's common stock in all Company plans. Directors who are appointed or elected to the Company's Board of Directors on a date other than that of the Annual Shareholder Meeting receive a pro-rata grant of such options, at an exercise price equal to the market price of the Company's common shares on the date of grant. At December 31, 2004, 74,000 options were available for grant under the 1995 Plan.

2001 Stock Option Plan The Company's 2001 Stock Option Plan, providing for nonqualified stock options and "incentive stock options," was approved by the Company's Board of Directors in October 2001. Under the 2001 Plan, 250,000 common shares are reserved for awards to officers of the Company, other key employees, non-employee directors, and advisors. Provisions of the 2001 Stock Option Plan include an automatic grant to each non-employee director of options to purchase up to 4,000 shares annually on the date of the Company's Annual Shareholder Meeting, at an exercise price equal to the market price of the Company's common shares on that date, until the non-employee director has options for a total of 12,000 shares of the Company's common stock in all Company plans. Directors who are appointed or elected to the Company's Board of Directors on a date other than that of the Annual Shareholder Meeting receive a pro-rata grant of such options, at an exercise price equal to the market price of the Company's common shares on the date of grant. As of December 31, 2004, no stock options had been granted under the 2001 Stock Option Plan, as there are still options available under the 1995 Plan.

Changes in options outstanding under the Stock Option Plans from January 1, 2002 to December 31, 2004 are as follows:

	Number of Options	Weighted Average Exercise Price
Balance at January 1, 2002	228,000	\$1.943
Exercised	(40,000)	\$1.631
Balance at December 31, 2002	188,000	\$2.156
Granted	11,000	\$5.272
Exercised	(10,000)	\$2.400
Forfeited	(5,000)	\$4.100
Repurchased	(5,000)	\$3.000
Balance at December 31, 2003	179,000	\$2.269
Granted	26,000	\$5.475
Exercised	(15,000)	\$2.478
Forfeited	(10,000)	\$5.717
Repurchased	(12,000)	\$3.494
Balance at December 31, 2004	168,000	\$2.560

The weighted average fair value of the options granted in 2004 was \$1.88.

Shares and Options Issued to Officer On August 15, 1995, the Company's Chairman and Chief Executive Officer was granted a ten-year, immediately exercisable option to purchase 1,495,000 common shares for an exercise price of \$.01 per share for which the Company recorded compensation expense of \$2,414,000. These options were granted to the officer as final consideration for personal guarantees of credit facilities and for continued employment with the Company. The officer exercised 846,000, 125,000 and 260,000 options during 2004, 2003 and 2002 respectively. The exercise in 2004 resulted in a \$944,000 increase to additional paid in capital and a \$1,540,000 increase in deferred tax assets. In 2003 the exercise resulted in a \$163,000 increase to additional paid in capital and a \$244,000 increase in deferred tax assets, and in 2002 the exercise resulted in a \$158,000 increase in additional paid in capital and a \$158,000 increase in deferred tax assets.

The following table summarizes information about all options outstanding at December 31, 2004:

Range of Exercise Prices	Options Outstanding			Options Exercisable	
	Number Outstanding	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price
\$0.010–0.010	264,000	0.67	\$0.010	264,000	\$0.010
1.625–1.688	100,000	0.67	1.626	100,000	1.626
3.000–4.100	43,000	4.77	3.189	43,000	3.189
4.570–6.050	24,000	9.03	5.284	4,000	4.570
\$0.010–6.050	431,000	1.60	\$1.000	411,000	\$0.782

At December 31, 2004 and 2003, 411,000 and 1,280,000 options, respectively, were vested and exercisable. Options issued to non-employee directors vest one year after their issuance. The vesting period for all other options issued under the Company's plans is determined by the Board of Directors at the time the options are issued. Options awarded to employees during 2003 and 2004 vest between one and five years.

Pro Forma Information related to Option Grants Pro forma information regarding net income and earnings per share is required by SFAS 123 for awards granted after December 31, 1995, as if the Company had accounted for its stock-based awards to employees under the fair value method of SFAS 123. The fair value of the Company's stock-based awards to employees was estimated using a Black-Scholes option pricing model. The Black-Scholes options valuation model was developed for use in estimating the fair value of traded options which have no vesting restrictions and are fully transferable. In addition, the Black-Scholes model requires the input of highly subjective assumptions including the expected stock price volatility. Because the Company's stock-based awards to employees have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its stock-based awards to employees. The effects of applying SFAS No. 123 in the proforma disclosure are not indicative of future amounts. The fair value of the Company's option grants under the 1984 and 1995 Plans was estimated assuming a dividend yield of 3.0% and the following weighted-average assumptions:

	2004	2003	2002*
Expected life (years)	10.0	10.0	N/A
Expected volatility	37.0%	29.0%	N/A
Risk-free interest rate	4.5%	4.3%	N/A

* Weighted-average assumptions are not applicable in 2002 because there were no options granted during the period ended December 31, 2002.

Repurchase of Common Stock, Common Stock Warrants and Stock Options In 1999 and 2001, the Board of Directors approved resolutions authorizing the Company to repurchase up to a total of 1,000,000 shares of its own stock on the open market. There were no shares repurchased on the open market during the years ending December 31, 2002 through December 31, 2004. The Company repurchased 42,000 common shares from the Company's Chairman and Chief Executive Officer during the year ending December 31, 2002. As the Company's stock has no par value, the entire repurchase price of the stock is recorded as a reduction to common stock.

In 2004 and 2003, the Company repurchased 12,000 and 5,000 options respectively under the 1995 stock option plan from former employees. The repurchase of the options is recorded as a reduction in additional paid-in-capital.

Dividends In January, April, July and October of 2004 the Company paid dividends of \$0.04, \$0.04, \$0.0425 and \$0.045 per share respectively. In December 2004 the Company declared dividends of \$0.045 per share, payable in January 2005. The Company paid dividends of \$0.16 per share and \$0.12 per share in the years ended December 31, 2003 and December 31, 2002, respectively.

NOTE 8—RETIREMENT PLAN

In 2002, the Company amended its defined-contribution retirement plan (the "Plan") to allow for a matching safe harbor contribution. For 2004, the Board of Directors elected to match participant deferred salary contributions up to a maximum of 4% of the participant's annual compensation. Matching contributions must be invested in shares of the Company's stock. Discretionary profit sharing contributions are allowed under the Plan in years that the Board does not elect a safe harbor match. The Company contributed \$33,000 and \$38,000 to the Plan for the safe harbor match for the years ended December 31, 2003 and December 31, 2002, respectively, and has accrued \$35,000 for the estimated safe harbor matching contribution for the year ended December 31, 2004.

NOTE 9—OPERATING LEASES

The Company leases office space and equipment under operating leases expiring at various dates through 2006.

Future minimum payments under noncancelable operating leases having initial terms of more than one year consisted of the following at December 31, 2004:

Year ending December 31,	
2005	303,000
2006	199,000
	\$502,000

Payments for repair and maintenance agreements incorporated in operating lease agreements are included in the future minimum operating lease payments shown above.

Rent expense was \$323,000, \$315,000, and \$350,000 for the years ended December 31, 2004, 2003 and 2002, respectively, and includes the above operating leases as well as month-to-month rental and certain executory costs.

The Company subleases a portion of its office space to two third parties for approximately \$2,000 per month under sub-sublease agreements that expire in May 2006.

In 2001 The Company entered into an agreement to sublease office space that expired in September 2002. Rental income received under this agreement was \$170,000 for the year ended December 2002.

NOTE 10—COMMITMENTS AND CONTINGENCIES

Under the terms of existing Gamma Knife quotation agreements, the Company is committed to purchase Gamma Knife equipment for \$7,630,000 when the equipment is placed in service at each customer location. At December 31, 2004, the Company had \$3,790,000 in deposits related to these purchase commitments which are classified as construction in progress.

NOTE 11—MAJOR CUSTOMERS

Revenues from the Company's Gamma Knife segment were provided by eighteen customers in 2004, seventeen customers in 2003, and fourteen customers in 2002.

In 2004 and 2003 no individual customers exceeded 10% of the Company's total revenue. In 2002, revenue from two individual customers of \$1,709,000 and \$1,614,000, respectively, exceeded 10% of the Company's total revenue.

NOTE 12—SUBSEQUENT EVENTS

The Company's 19th Gamma Knife unit, a 10 year turn-key retail contract at Baptist Hospital of East Tennessee, became operational in January 2005.

To the Board of Directors and Shareholders

American Shared Hospital Services

We have audited the accompanying consolidated balance sheets of American Shared Hospital Services as of December 31, 2004 and 2003, and the related consolidated statements of operations, shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2004. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board of the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of American Shared Hospital Services at December 31, 2004 and 2003, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2004 in conformity with U.S. generally accepted accounting principles.



San Francisco, California

January 21, 2005

MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

The Company's common shares, no par value (the "Common Shares"), are currently traded on the American Stock Exchange and the Pacific Exchange. The table below sets forth the high and low closing sale prices of the Common Shares of the Company on the American Stock Exchange Consolidated Reporting System for each full quarter for the last two fiscal years.

PRICES FOR COMMON SHARES

Quarter Ending	High	Low
March 31, 2003	\$4.21	\$3.55
June 30, 2003	\$5.20	\$3.75
September 30, 2003	\$6.15	\$4.78
December 31, 2003	\$6.83	\$5.33
March 31, 2004	\$7.79	\$5.55
June 30, 2004	\$7.24	\$5.35
September 30, 2004	\$5.62	\$4.25
December 31, 2004	\$6.15	\$4.70

The Company estimates that there were approximately 2,500 beneficial holders of its Common Shares at December 31, 2004.

The Board of Directors authorized in March 1999 the repurchase of up to 500,000 shares of the Company's Common Stock in the open market from time to time at prevailing prices. Approximately 484,000 shares have been repurchased in the open market pursuant to that authorization at a cost of approximately \$1,213,000, although no shares have been repurchased since 2001. The Board of Directors on February 2, 2001 authorized the repurchase of up to another 500,000 shares of the Company's common stock in the open market from time to time at prevailing prices. No shares have been repurchased under this additional authorization.

During 2004 holders of options to acquire the Company's common stock exercised their respective rights pursuant to such securities, resulting in the Company issuing 858,000 new shares of common stock for approximately \$40,000.

On March 22, 1999 the Company adopted a Shareholder Rights Plan ("Plan"). Under the Plan, the Company made a dividend distribution of one Right for each outstanding share of the Company's common stock as of the close of business on April 1, 1999. The Rights become exercisable only if any person or group, with certain exceptions, becomes an "acquiring person" (acquires 15 percent or more of the Company's outstanding common stock) or announces a tender or exchange offer to acquire 15 percent or more of the Company's outstanding common stock. The Company's Board of Directors adopted the Plan to protect shareholders against a coercive or inadequate takeover offer. The Board of Directors is not aware that any person or group intends to make a takeover offer for the Company.

At December 31, 2004 the Company had 4,776,173 issued and outstanding common shares, 755,627 common shares reserved for options, and 5,208 shares reserved pursuant to the Company's Shareholder Rights Plan.

In fourth quarter 2004, the Board of Directors declared a quarterly dividend of \$.045 per common share to shareholders of record on January 3, 2005, paid on January 14, 2005. During 2004, shareholders of record as of January 2, 2004, April 2, 2004, July 2, 2004 and October 1, 2004 were paid quarterly dividends respectively as follows: \$0.04 on January 15, 2004, \$0.04 on April 16, 2004, \$0.0425 on July 15, 2004, and \$0.045 on October 15, 2004. The Board of Directors anticipates declaring and paying quarterly cash dividends in similar amounts in the future subject to evaluation of the Company's level of earnings, balance sheet position and availability of cash. The Company did not pay cash dividends prior to 2001.

CORPORATE INFORMATION

CORPORATE HEADQUARTERS

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American Stock Transfer & Trust Company
59 Maiden Lane, Plaza Level
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INDEPENDENT AUDITORS

Moss Adams LLP
Stockton, CA

COUNSEL

Davis Polk & Wardwell
Menlo Park, CA

ANNUAL SHAREHOLDERS' MEETING

June 16, 2005
9:00 AM Pacific Time
The Ritz Carlton
600 Stockton Street
San Francisco, CA 94108

FORM 10-K

A copy of our annual report on Form 10-K as filed with the Securities and Exchange Commission may be obtained without charge by contacting us at 415.788.5300.

DIRECTORS

Ernest A. Bates, M.D.
Chairman of the Board

Ernest R. Bates
Managing Director
HSBC Securities, Inc.
San Francisco, CA

Olin C. Robison
President
Salzburg Seminar
Middlebury, VT

John F. Ruffle
Retired Former
Vice-Chairman of the Board
J.P. Morgan & Co. Inc.
New York, NY

Stanley S. Trotman, Jr.
Retired Former Managing
Director
Healthcare Group
PaineWebber Incorporated
New York, NY

OFFICERS

Ernest A. Bates, M.D.
Chief Executive Officer

Craig K. Tagawa
Chief Operating Officer
Chief Financial Officer

Norman A. Houck
Vice President
Controller

Willie R. Barnes
Corporate Secretary

This annual report may be deemed to contain certain forward-looking statements with respect to the financial condition, results of operations and future plans of American Shared Hospital Services, which involve risks and uncertainties including, but not limited to, the risks of the Gamma Knife business and the risks of developing its IMRT, Operating Room for the 21st Century® and tax-exempt operating lease programs. Further information on potential factors that could affect the financial condition, results of operations and future plans of American Shared Hospital Services is included in the filings of the Company with the Securities and Exchange Commission, including the Company's Annual Report on Form 10-K for the year ended December 31, 2004 and the definitive Proxy Statement for the Annual Meeting of Shareholders held on June 16, 2005.

AMERICAN SHARED HOSPITAL SERVICES

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