



Expanding our

Growth

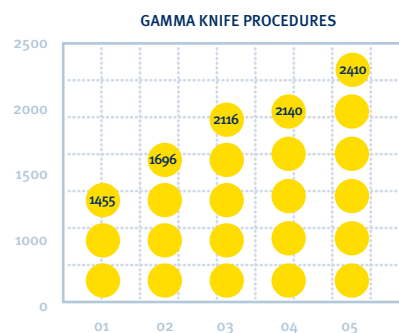
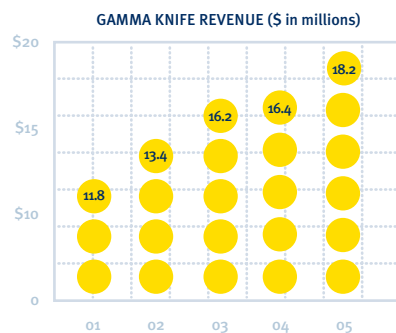
AMERICAN
SHARED
HOSPITAL
SERVICES



Expanding^{our} Growth

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Fiscal 2005 marked the beginning of a new era for American Shared Hospital Services. In addition to continuing our record-breaking performance, we are expanding into a new technology that is widely regarded as the next evolutionary step in radiation therapy. This venture positions us for accelerated growth in the years to come.

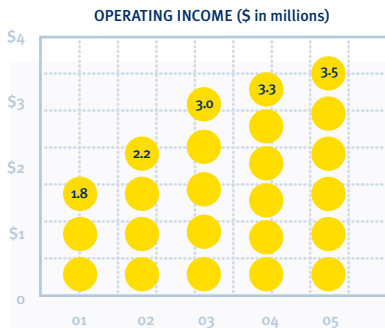


This is an exhilarating time for American Shared Hospital Services. I am delighted to report that 2005 was our best year ever. Our Gamma Knife business continued to flourish, resulting in record operating income and revenues – as well as another dividend increase for our shareholders.

Just as important, our efforts to pursue new technological and partnering opportunities have come to fruition. We have acquired an equity interest in Still River Systems Inc., developers of the Clinatron 250®, a new Proton Beam Therapy (PBT) system. PBT is considered by many to be the superior cancer treatment modality. However, until now, the cost of PBT has been prohibitive for all

T O U R S H A R E H O L D E R S

but a few institutions. According to Still River, this device is designed to deliver comparable results to other PBT systems costing over \$100 million, but at a significantly lower cost. We anticipate strong interest in this new alternative when it becomes available, particularly when combined with our creative financing solutions.



Turning to our 2005 results, our operating income climbed to almost \$3.5 million – a 6% increase over fiscal 2004. In addition, our revenues grew 11% over 2004 to \$18.2 million. Further, our annual dividend payment increased from 16-¾ cents to 18-½ cents, and our common share price rose from \$5.95 to \$6.28 – resulting in an 8.7% total shareholder return. Looking back, our dividends have increased 85% since they began at 10 cents annually in 2001.

We attribute these outstanding results to the continuing success of our Gamma Knife business, which has benefited from our ongoing focus on effective management and cost control. We opened three new Gamma Knife centers in 2005, bringing us to 21 facilities nationwide. We anticipate continued Gamma Knife revenue growth in 2006, and also have plans for further expansion into new technologies in order to ensure our ongoing success.

The coming years promise to be an exciting and rewarding time for us. We look forward to updating you on our achievements.

Ernest A. Bates, M.D. Chairman & Chief Executive Officer April 7, 2006

Building on our Core Business


GAMMA KNIFE
IMRT
IGRT
PROTON BEAM
OR21



American Shared is proud to be the leader in alternative financing for Gamma Knife units. Since 1991, American Shared's creative financing solutions have enabled our current twenty-one clinical partners to open state-of-the-art Gamma Knife centers nationwide – and our strategic planning and marketing assistance have helped ensure each center's success.

Our unique fee-for-service financing could also benefit hospitals that want to acquire other technologies, such as Intensity Modulated Radiation Therapy (IMRT) and Image-Guided Radiation Therapy (IGRT). IGRT integrates tumor imaging and detection components into a linear accelerator – allowing clinicians to plan treatment, verify positioning, and deliver treatment with a single device. This means faster, more effective radiation therapy with less damage to healthy tissue.

We are currently exploring an expanded IMRT/IGRT financial model that would include treatment simulation and planning equipment and software – resulting in a complete, state-of-the-art radiation therapy department. This model also contemplates the joint development of satellite radiation therapy centers with our clinical partners.



With American Shared's help, hospitals nationwide are improving patient outcomes through Gamma Knife, the leading non-invasive alternative to traditional brain surgery. Now, we're building on this core business by offering financing for even more advanced technologies – and exploring an expanded financial model to support complete, state-of-the-art radiation therapy departments.

Investing ⁱⁿ Innovation

OR21



Several years ago, American Shared had a truly innovative idea: to create a futuristic surgical suite featuring robotic technology, and then offer the financing solutions to make it a reality for our clinical partners. We are making great progress in realizing this goal. Many of the unique designs and processes we have developed with NBBJ – our architectural collaborator – now have patents pending.

The mission of our Operating Room for the 21st Century (OR21®) is to develop a cost-effective operating room that delivers improved clinical patient outcomes. The OR21 suite will feature state-of-the-art technologies such as:

- Intelligent lighting system operated through a chip in the surgeon's glove
- Diagnostic imaging equipment that provides real-time information during surgery
- Computer-controlled, motorized combination operating room table and ICU bed
- Robotic cross-cleaning systems with biocidal misting
- Flat panel monitors outside the surgical zone to check patient vital statistics and diagnostic images
- Voice-activated, robotic nursing assistance

As the OR21 design takes shape, we anticipate growing interest. With our help, institutions nationwide will be able to offer the latest in futuristic technologies today.



OR21 – our proprietary, futuristic surgical suite – will bring our clinical partners to the forefront of innovation. Suite design is now taking place, with patents pending on our unique technologies and processes. Our financing solutions will bring this concept to major medical centers with a minimal investment.

Seizing^{new}

Opportunities


PROTON
BEAM
THERAPY



For many years, Proton Beam Therapy (PBT) has been regarded as potentially the most effective cancer treatment available. PBT attacks tumors with *protons* instead of the photons used in conventional radiation therapy. Protons, which release almost all of their energy when they reach a specific depth, are far less toxic to normal tissues and deliver much higher radiation doses to tumors – critical factors in targeting tumors close to key areas and treating children.

Until now, PBT required multiple-story treatment facilities of three or more rooms, resulting in costs of over \$100 million and the need for a high volume of patients. Now, Still River Systems Inc. – in collaboration with MIT's Plasma Science and Fusion Center – has designed the Clinatron 250, which is not currently FDA approved. According to Still River, this new, more compact PBT system requires only one treatment room – significantly reducing both cost and patient volume requirements.

The potential magnitude of growth for the Clinatron 250 is very high. Yet even with its lower cost, hospitals will still need financing assistance. To capitalize on this opportunity, we are in the process of buying two Clinatron 250 systems to offer to clinical partners and have acquired an equity interest in Still River, which will position us to benefit directly from this product's future success.

A hand is shown from the palm side, with the index finger pointing upwards. A bright, glowing white square is superimposed over the tip of the index finger. The background is a dark blue grid of rounded squares. The bottom of the image is a solid yellow bar.

Proton Beam Therapy – long regarded as the technology of choice for cancer treatment – is now significantly more affordable due to a new product called the Clinatron 250.

With our investment in this product – and its developer – we are well-positioned to capitalize on this exceptional opportunity.

2005

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American Shared Hospital Services

SELECTED FINANCIAL DATA

SUMMARY OF OPERATIONS

	Year Ended December 31,				
	(Amounts in thousands except per share data)				
	2005	2004	2003	2002	2001
Medical services revenue	\$18,231	\$16,389	\$16,178	\$13,366	\$11,758
Costs of operations	9,072	7,887	7,400	5,399	4,285
Selling and administrative expense	3,613	2,963	3,255	3,313	3,245
Interest expense	2,075	2,261	2,547	2,437	2,456
Total costs and expenses	14,760	13,111	13,202	11,149	9,986
Income from operations	3,471	3,278	2,976	2,217	1,772
Interest and other income	202	102	121	171	480
Minority interest expense	(1,126)	(983)	(928)	(831)	(751)
Income before income taxes	2,547	2,397	2,169	1,557	1,501
Income tax expense	(780)	(412)	(787)	(455)	(433)
Net income	\$1,767	\$1,985	\$1,382	\$1,102	\$1,068
Net income per common share:					
Basic	\$ 0.36	\$ 0.46	\$ 0.36	\$ 0.30	\$ 0.30
Diluted	\$ 0.35	\$ 0.39	\$ 0.27	\$ 0.22	\$ 0.21
Cash dividend declared per common share	\$ 0.1875	\$ 0.1725	\$ 0.20	\$ 0.12	\$ 0.10
Dividend payout ratio (paid and declared)	0.54	0.44	0.74	0.55	0.48

See accompanying note

BALANCE SHEET DATA

	As of December 31,				
	(Amounts in thousands)				
	2005	2004	2003	2002	2001
Cash & cash equivalents	\$ 1,298	\$ 8,121	\$10,312	\$ 9,924	\$11,580
Securities – current	4,537	957	—	—	—
Restricted cash	50	50	50	50	50
Working capital	2,423	4,978	5,268	7,175	9,351
Securities – long term	2,797	—	—	—	—
Total assets	48,668	47,367	46,304	44,830	42,385
Current portion of long-term debt/capital leases	6,377	6,562	6,803	5,490	4,305
Long-term debt/capital leases less current portion	18,705	18,924	20,114	22,006	21,615
Shareholders' equity	\$18,320	\$17,546	\$15,329	\$14,540	\$13,785

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. 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 2001 through 2005.

American Shared Hospital Services

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 contracts with 15 fee per use hospitals and six 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 six agreements that are based on revenue sharing. These can be further classified as either "turn-key" arrangements or "net revenue sharing" arrangements. For the four 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.

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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 29%, 25% and 24% of revenue for the years ended December 31, 2005, 2004 and 2003, 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, 2005 changed by as much as 10% based on actual collection information, it would have the effect of increasing or decreasing revenue by approximately \$252,000.

GENERAL

During the years ended December 31, 2005, 2004 and 2003, 100% of the Company's revenue was derived from its Gamma Knife business.

TOTAL REVENUE

	2005	Increase (Decrease)	2004	Increase (Decrease)	2003
Medical services revenue (in thousands)	\$18,231	11.2%	\$16,389	1.3%	\$16,178
Number of Gamma Knife procedures	2,410	12.6%	2,140	1.1%	2,116
Average revenue per procedure	\$ 7,565	(1.2)%	\$ 7,658	0.2%	\$ 7,646

Medical services revenue increased 11.2% in 2005 compared to 2004 and increased 1.3% in 2004 compared to 2003. The increase in both 2005 and 2004 is due to an increase in the number of Gamma Knife units in operation. The Company had twenty-one, eighteen and seventeen Gamma Knife units in operation at December 31, 2005, 2004 and 2003, respectively.

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Gamma Knife revenue increased \$1,842,000 and \$211,000 in 2005 and 2004, respectively, compared to the prior years. The 2005 increase was due to three new Gamma Knife units that began operation during 2005 and the full year inclusion of one new Gamma Knife unit that began operation during 2004, which offset a 4% decrease in revenue from Gamma Knife units in operation more than one year. The 2004 increase compared to 2003 was primarily due to one new Gamma Knife units 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 number of Gamma Knife procedures in 2005 increased by 270 compared to 2004 due to the increase in the number of Gamma Knife units in operation, as well as a 3% increase in procedures from Gamma Knife units in operation more than one year. 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 from Gamma Knife units in operation more than one year.

Revenue per procedure decreased \$93 in 2005 and increased \$12 in 2004 compared to the prior years. 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. The decrease per procedure in 2005 is primarily due to lower average procedure rates collected at two of the Company's retail sites.

COSTS OF OPERATIONS

(In thousands)	2005	Increase	2004	Increase	2003
Costs of operations	\$9,072	15.0%	\$7,887	6.6%	\$7,400
Percentage of revenue	49.8%		48.1%		45.7%

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 \$1,185,000 in 2005 compared to 2004, and increased \$487,000 in 2004 compared to 2003.

The Company's maintenance and supplies costs were 6%, 5% and 5% of medical service revenue in 2005, 2004 and 2003, respectively. Maintenance and supplies costs increased \$150,000 in 2005 compared to 2004, and increased \$139,000 in 2004 compared to 2003. The increase in 2005 compared to 2004 was primarily due to the expiration of the warranty period on one Gamma Knife unit and the full year inclusion of maintenance on two Gamma Knife units whose warranty period expired during the previous year. 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.

Depreciation and amortization increased \$593,000 in 2005 compared to 2004, and increased \$577,000 in 2004 compared to 2003. The increase in 2005 was primarily due to the addition of three new Gamma Knife units that commenced operation during first, second and third quarters of 2005 and a full year of depreciation on one new Gamma Knife units that started operation during 2004. 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.

Other direct operating costs as a percentage of medical services revenue were 14%, 13% and 15% in 2005, 2004 and 2003, respectively. The increase of \$442,000 in 2005 compared to 2004 was primarily due to increased operating costs related to the Company's two additional retail Gamma Knife units that started operation during 2005 and higher insurance costs due to additional

American Shared Hospital Services

Gamma Knife units in operation, which were partially offset by lower marketing and promotion costs. 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.

SELLING AND ADMINISTRATIVE

(In thousands)	2005	Increase (Decrease)	2004	Increase (Decrease)	2003
Selling and administrative costs	\$3,613	21.9%	\$2,963	(9.0)%	\$3,255
Percentage of revenue	19.8%		18.1%		20.1%

The Company's selling and administrative costs increased \$650,000 in 2005 compared to 2004, and decreased \$292,000 in 2004 compared to 2003. The increase in 2005 compared to 2004 was primarily due to increased payroll and business development costs of approximately \$441,000, which included costs of the Company's second Gamma Knife User's Meeting of approximately \$42,000 and OR21 business development costs of approximately \$151,000. In addition, legal, accounting and consulting fees increased approximately \$119,000 and contributions increased approximately \$55,000 over the prior year. 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.

INTEREST EXPENSE

(In thousands)	2005	Increase (Decrease)	2004	Increase (Decrease)	2003
Interest expense	\$2,075	(8.2)%	\$2,261	(11.2)%	\$2,547
Percentage of revenue	11.4%		13.8%		15.7%

The Company's interest expense decreased \$186,000 in 2005 compared to 2004, and decreased \$286,000 in 2004 compared to 2003. The decrease in 2005 was due to lower interest expense on the Company's more mature Gamma Knife units and the completion of debt service on two Gamma Knife units. This was partially offset by additional interest expense on the financing of the Company's three new Gamma Knife units that started operation during 2005, and the refinancing of one Gamma Knife unit that had previously been paid off. 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. Fourteen of the Company's twenty-one Gamma Knife units have been in operation for more than three years and generally have significantly lower interest expense than newer units because interest expense decreases with each principal payment.

OTHER INCOME AND EXPENSE

(In thousands)	2005	Increase (Decrease)	2004	Increase (Decrease)	2003
Interest and other income	\$202	98.0%	\$102	(15.7)%	\$121
Percentage of revenue	1.1%		0.6%		0.7%
Minority interest expense	\$(1,126)	14.5%	\$(983)	5.9%	\$(928)
Percentage of revenue	(6.2)%		(6.0)%		(5.7)%

Interest and other income increased \$100,000 in 2005 compared to 2004 and decreased \$19,000 in 2004 compared to 2003. The increase in 2005 was primarily due to investment in longer term holdings with higher interest rates available compared to 2004. The decrease in 2004 was primarily due to lower invested cash balances during 2004.

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Minority interest increased \$143,000 in 2005 and \$55,000 in 2004 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)	2005	Increase (Decrease)	2004	Increase (Decrease)	2003
Income tax expense	\$780	89.3%	\$412	(47.6%)	\$787
Percentage of revenue	4.3%		2.5%		4.9%

Income tax expense increased \$368,000 in 2005 compared to 2004, and decreased \$375,000 in 2004 compared to 2003. The Company's estimated 37% effective income tax provision for 2005 was reduced by a \$193,000 income tax benefit from the exercise of options to purchase 264,000 common shares. 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 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, 2005 of approximately \$12,556,000.

NET INCOME

(In thousands, except per share amounts)	2005	Increase (Decrease)	2004	Increase (Decrease)	2003
Net income	\$1,767	(11.0)%	\$1,985	43.6%	\$1,382
Net income per share, diluted	\$ 0.35	(10.3)%	\$ 0.39	44.4%	\$ 0.27

The Company had net income of \$1,767,000 in 2005 compared to \$1,985,000 in 2004 and \$1,382,000 in 2003. Net income for 2005 included increased operating income of \$193,000 compared to 2004, which was primarily due to the addition of three new Gamma Knife units during 2005. This was offset by an increase in income tax expense of \$368,000 due to reduced income tax benefits available on the exercise of options to purchase common stock. 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.

LIQUIDITY AND CAPITAL RESOURCES

The Company had cash and cash equivalents of \$1,298,000 at December 31, 2005 compared to \$8,121,000 at December 31, 2004. This decrease in cash resulted primarily from the Company's decision during 2005 to invest an additional \$6,377,000 of its available cash into marketable securities. 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.

American Shared Hospital Services

Securities represents a portion of the Company's cash that is invested in high-quality short to long-term fixed income marketable securities in order to maximize income on its available cash. Securities with maturity dates between three and twelve months in the amount of \$4,537,000 are classified as current assets. Securities in the amount of \$2,797,000 have maturities in excess of one year and are classified as long-term. It is the Company's intent to hold these securities until maturity.

Restricted cash of \$50,000 at December 31, 2005 reflects cash that may only be used for the operations of GKF.

Operating activities provided cash of \$8,480,000 in 2005. Net income of \$1,767,000, depreciation and amortization of \$5,502,000 and an increase in the minority interest of \$1,126,000 were the primary reasons for the increase in operating cash flow. The Company's trade accounts receivable increased to \$3,832,000 at December 31, 2005 from \$2,793,000 at December 31, 2004, which was primarily due to the addition of three new Gamma Knife contracts during 2005, two of which were retail contracts, and an increase in the number of days revenue outstanding ("DSO") in accounts receivable for some of the Gamma Knife contracts. The DSO was 76 and 66 days as of December 31, 2005 and December 31, 2004, 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.

Investing activities used \$12,572,000 of cash in 2005 primarily due to an investment in short to long-term securities of \$7,334,000 and for the acquisition of property and equipment of \$6,195,000, primarily for the three Gamma Knife units that became operational during 2005.

Financing activities used \$2,731,000 of cash during 2005, primarily due to principal payments on long-term debt of \$7,419,000, distributions to minority owners of \$912,000 and the payment of dividends of \$902,000. This was partially offset by financing on the acquisition of property and equipment of \$7,015,000, primarily for the three Gamma Knife units that became operational during 2005.

Working capital decreased \$2,555,000 to \$2,423,000 at December 31, 2005 from \$4,978,000 at December 31, 2004 primarily due to a decrease in cash and current securities of \$3,243,000 which was partially offset by an increase in trade accounts receivable of \$1,039,000.

The Company primarily invests its cash in money market or similar funds and high quality short to long-term securities in order to minimize the potential for principal erosion. Cash is invested in these 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 2006.

The Company finances all of its Gamma Knife units, and anticipates that it will continue to do so with future contracts. During 2003 the Company's primary lender, DVI, filed for Chapter 11 bankruptcy protection. The principal balance of notes held by DVI were transferred to a third party lender as successor servicer, and the Company continues to make payments on the outstanding note balances serviced by this third party lender. The Company has secured financing for its recent projects from other lenders and anticipates that it will be able to secure financing on future projects from these or other lending sources, but there can be no assurance that financing will continue to be available on acceptable 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.

American Shared Hospital Services

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

The following table presents, as of December 31, 2005, 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.

<i>Contractual Obligations</i>	Payments Due by Period				
	Total amounts committed	Less than 1 year	1-3 years	4-5 years	After 5 years
Long-term debt	\$20,884,000	\$5,631,000	\$12,619,000	\$2,634,000	
Capital Leases	4,198,000	746,000	2,331,000	1,013,000	\$108,000
Future Gamma Knife purchases ⁽¹⁾	2,109,000		2,109,000		
Operating leases	235,000	208,000	27,000		
Total contractual obligations	\$27,426,000	\$6,585,000	\$17,086,000	\$3,647,000	\$108,000

(1) The Company has deposits toward the upgrade and reload of certain Gamma Knife units already in service. The term financing for these upgrades will not be finalized until 2006, and therefore an accurate determination of payments by period cannot be made as of December 31, 2005. 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, capital leases in Note 9, and operating leases in Note 10 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, 2005. 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.

(In thousands)	Maturity Date, Year ending December 31						Total	Fair Value
	2006	2007	2008	2009	2010	Thereafter		
Fixed-rate long-term debt and present value of capital leases	\$6,377	\$5,674	\$4,732	\$4,544	\$2,477	\$1,278	\$25,082	\$25,088
Average interest rates	8.6%	8.4%	8.2%	8.1%	7.9%	7.8%	8.3%	

At December 31, 2005, we had no significant long-term, market-sensitive investments.

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,	
	2005	2004
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$ 1,298,000	\$ 8,121,000
Securities	4,537,000	957,000
Restricted cash	50,000	50,000
Trade accounts receivable, net of allowance for doubtful accounts of \$170,000 in 2005 and \$170,000 in 2004	3,832,000	2,793,000
Other receivables	187,000	157,000
Prepaid expenses and other current assets	464,000	594,000
Current deferred tax assets	341,000	261,000
Total current assets	10,709,000	12,933,000
PROPERTY AND EQUIPMENT, net	34,990,000	34,272,000
SECURITIES	2,797,000	—
OTHER ASSETS	172,000	162,000
	\$48,668,000	\$47,367,000
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES		
Accounts payable	\$ 555,000	\$ 282,000
Accrued interest and other liabilities	996,000	808,000
Employee compensation and benefits	120,000	88,000
Accrued dividends	238,000	215,000
Current portion of long-term debt	5,631,000	6,562,000
Current portion of long-term capital leases	746,000	—
Total current liabilities	8,286,000	7,955,000
LONG-TERM DEBT, less current portion	15,253,000	18,924,000
LONG-TERM CAPITAL LEASES, less current portion	3,452,000	—
DEFERRED INCOME TAXES	828,000	627,000
MINORITY INTEREST	2,529,000	2,315,000
SHAREHOLDERS' EQUITY		
Common stock, no par value		
Authorized—10,000,000 shares		
Issued and outstanding shares—5,019,000 in 2005 and 4,776,000 in 2004	9,306,000	9,238,000
Additional paid-in capital	4,274,000	4,410,000
Retained earnings	4,740,000	3,898,000
Total shareholders' equity	18,320,000	17,546,000
	\$48,668,000	\$47,367,000

See accompanying notes

American Shared Hospital Services

CONSOLIDATED STATEMENTS OF INCOME

	Years Ended December 31,		
	2005	2004	2003
REVENUE:			
Medical services	\$18,231,000	\$16,389,000	\$16,178,000
COSTS AND EXPENSES:			
Costs of revenue:			
Maintenance and supplies	1,035,000	885,000	746,000
Depreciation and amortization	5,395,000	4,802,000	4,225,000
Other direct operating costs	2,642,000	2,200,000	2,429,000
	9,072,000	7,887,000	7,400,000
GROSS MARGIN	9,159,000	8,502,000	8,778,000
Selling and administrative expense	3,613,000	2,963,000	3,255,000
Interest expense	2,075,000	2,261,000	2,547,000
Operating income	3,471,000	3,278,000	2,976,000
Interest and other income	202,000	102,000	121,000
Minority interest expense	(1,126,000)	(983,000)	(928,000)
Income before income taxes	2,547,000	2,397,000	2,169,000
Income tax expense	(780,000)	(412,000)	(787,000)
NET INCOME	\$ 1,767,000	\$ 1,985,000	\$ 1,382,000
Earnings per common share—basic	\$0.36	\$0.46	\$0.36
Earnings per common share—diluted	\$0.35	\$0.39	\$0.27

See accompanying notes

American Shared Hospital Services

CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY

Three Years Ended December 31,

	Common Shares	Common Stock	Additional Paid-in Capital	Retained Earnings	Total
Balances at January 1, 2003	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 stock 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	9,198,000	4,410,000	3,898,000	17,546,000
Options exercised	357,000	157,000	445,000	—	602,000
Common stock withheld on option exercises	(114,000)	(89,000)	(581,000)	—	(670,000)
Dividends	—	—	—	(925,000)	(925,000)
Net income	—	—	—	1,767,000	1,767,000
Balances at December 31, 2005	5,019,000	\$9,306,000	\$4,274,000	\$4,740,000	\$18,320,000

See accompanying notes

American Shared Hospital Services

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Years Ended December 31,		
	2005	2004	2003
OPERATING ACTIVITIES			
Net income	\$ 1,767,000	\$ 1,985,000	\$ 1,382,000
Adjustments to reconcile net income to net cash from operating activities:			
Depreciation and amortization	5,502,000	4,892,000	4,313,000
Deferred income tax	121,000	264,000	669,000
Minority interest in consolidated subsidiaries	1,126,000	983,000	928,000
Changes in operating assets and liabilities:			
Receivables	(1,069,000)	(483,000)	104,000
Prepaid expenses and other assets	95,000	(137,000)	426,000
Accounts payable and accrued liabilities	938,000	104,000	318,000
Net cash from operating activities	8,480,000	7,608,000	8,140,000
INVESTING ACTIVITIES			
Payment for purchase of property and equipment	(6,195,000)	(6,308,000)	(5,929,000)
Proceeds from sales and maturities of marketable securities	957,000	—	—
Investment in marketable securities	(7,334,000)	(957,000)	—
Net cash from investing activities	(12,572,000)	(7,265,000)	(5,929,000)
FINANCING ACTIVITIES			
Principal payments on long-term debt	(7,122,000)	(7,371,000)	(5,777,000)
Principal payments on capital leases	(297,000)	—	—
Long term debt financing on purchase of property and equipment	5,275,000	5,940,000	5,198,000
Capital lease financing	1,740,000	—	—
Payment of dividends	(902,000)	(699,000)	(610,000)
Distributions to minority owners	(912,000)	(399,000)	(645,000)
Proceeds from exercise of stock options	157,000	40,000	25,000
Repurchase of stock options	(670,000)	(45,000)	(14,000)
Net cash from financing activities	(2,731,000)	(2,534,000)	(1,823,000)
Net increase (decrease) in cash and cash equivalents	(6,823,000)	(2,191,000)	388,000
CASH AND CASH EQUIVALENTS, beginning of year	8,121,000	10,312,000	9,924,000
CASH AND CASH EQUIVALENTS, end of year	\$ 1,298,000	\$ 8,121,000	\$ 10,312,000
SUPPLEMENTAL CASH FLOW DISCLOSURE			
Interest paid	\$ 2,075,000	\$ 2,500,000	\$ 2,692,000
Income taxes paid	\$ 229,000	\$ 129,000	\$ 88,000
SCHEDULE OF NONCASH INVESTING AND FINANCING ACTIVITIES			
Accrued dividends	\$ 238,000	\$ 215,000	\$ 157,000
Income tax benefit from stock option exercise recorded to Additional paid-in capital	\$ 445,000	\$ 994,000	\$ 163,000

See accompanying notes

American Shared Hospital Services

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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 twenty-one medical centers in Arkansas, California, Connecticut, Florida, Illinois, Maryland, Massachusetts, Mississippi, Nevada, New Jersey, New Mexico, New York, Ohio, Oklahoma, Pennsylvania, Tennessee, 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 alternative financing arrangements, such as fee-for-service lease arrangements with health care institutions in the United States and Brazil.

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 accounting principles generally accepted in the United States of America, 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 long term fixed income marketable 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, 2005, the cost of these securities approximated fair market value, and they ranged in maturity up to approximately eighteen months. The value of those securities with maturity dates greater than one year are considered long-term securities and are classified accordingly on the balance sheet.

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

Business and credit risk The Company maintains its cash balances, which exceed federally insured limits, in financial institutions. Additionally the Company’s securities are invested in short to long 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.

American Shared Hospital Services

All of the Company's revenue is provided by twenty-one customers. These customers constitute accounts receivable at December 31, 2005. 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 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 \$17,000 and \$94,000 in 2005 and 2004, 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, 2005, the Company held equipment under operating lease contracts with customers with an original cost of \$55,348,000 and accumulated depreciation of \$24,074,000. 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.

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, 2005, 2004 and 2003.

American Shared Hospital Services

	2005	2004	2003
Numerator for basic and diluted earnings per share	\$1,767,000	\$1,985,000	\$1,382,000
Denominator:			
Denominator for basic earnings per share— weighted-average shares	4,931,000	4,351,000	3,850,000
Effect of dilutive securities Employee stock options	160,000	750,000	1,238,000
Denominator for diluted earnings per share— adjusted weighted-average shares	\$5,091,000	\$5,101,000	\$5,088,000
Earning per share—basic	\$ 0.36	\$ 0.46	\$ 0.36
Earning per share—diluted	\$ 0.35	\$ 0.39	\$ 0.27

In 2005, options outstanding to purchase 76,000 shares of common stock at an exercise price of \$6.16 - \$6.45 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 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.

Reclassifications Certain reclassifications have been made to the 2004 balances to conform with the 2005 presentation.

Stock-based compensation The Company had in effect two stock-based employee compensation plans during 2005, 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,		
	2005	2004	2003
Net income, as reported	\$1,767,000	\$1,985,000	\$1,382,000
Deduct: total stock-based employee compensation expense determined under fair value based method for all awards (Note 7), net of related tax effects	(36,000)	(9,000)	(3,000)
Proforma net income	\$1,731,000	\$1,976,000	\$1,379,000
Earnings per share:			
Basic—as reported	\$ 0.36	\$ 0.46	\$ 0.36
Basic—pro forma	\$ 0.35	\$ 0.45	\$ 0.36
Diluted—as reported	\$ 0.35	\$ 0.39	\$ 0.27
Diluted—pro forma	\$ 0.34	\$ 0.39	\$ 0.27

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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, 2005 and 2004 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 \$25,088,000 and \$25,637,000 at December 31, 2005 and 2004, 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 first quarter 2006. 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,	
	2005	2004
Medical equipment and facilities	\$ 59,147,000	\$ 49,336,000
Office equipment	549,000	438,000
Deposits and construction in progress	703,000	4,499,000
	60,399,000	54,273,000
Accumulated depreciation	(25,409,000)	(20,001,000)
Net property and equipment	\$ 34,990,000	\$ 34,272,000

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As of December 31, 2005, the Company has equipment that is secured under capitalized leases with a total cost of approximately \$8,545,000, which is included in Medical equipment and facilities, and associated accumulated depreciation totaling approximately \$4,027,000.

NOTE 4—LONG-TERM DEBT

Long-term debt consists primarily of 19 notes with financing companies, related to Gamma Knife construction and installation, totaling \$20,884,000. These notes accrue interest at fixed annual rates between 7.98% and 10.95%, are payable in 60 to 84 monthly installments, mature between March 2006 and April 2012, and are collateralized by the respective Gamma Knife units. As of December 31, 2005 and December 31, 2004 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, 2005:

Year ending December 31,	
2006	\$ 5,631,000
2007	4,867,000
2008	3,859,000
2009	3,893,000
2010	1,990,000
Thereafter	644,000
	\$20,884,000

NOTE 5—INCOME TAXES

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

	December 31,	
	2005	2004
Deferred tax liabilities:		
Fixed assets	\$(5,641,000)	\$(5,548,000)
Total deferred tax liabilities	(5,641,000)	(5,548,000)
Deferred tax assets:		
Net operating loss carryforwards	4,307,000	4,418,000
Accrued reserves	276,000	263,000
Other—net	571,000	501,000
Total deferred tax assets	5,154,000	5,182,000
Net deferred tax liabilities	\$ (487,000)	\$ (366,000)

These amounts are presented in the financial statements as follows:

	December 31,	
	2005	2004
Current deferred tax assets	\$341,000	\$261,000
Deferred income taxes (non-current)	(828,000)	(627,000)
	\$ (487,000)	\$ (366,000)

American Shared Hospital Services

The 2005 and 2004 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 \$616,000 and \$1,540,000 for 2005 and 2004 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,		
	2005	2004	2003
Current: Federal	\$449,000	—	—
State	210,000	47,000	38,000
Total current	659,000	47,000	38,000
Deferred: Federal	(74,000)	296,000	649,000
State	195,000	69,000	100,000
Total deferred	121,000	365,000	749,000
	\$780,000	\$412,000	\$787,000

The provision for income taxes differs from the amount computed by applying the U.S. federal statutory tax rate (34% in 2005, 2004 and 2003) to income before taxes as follows:

	Years Ended December 31,		
	2005	2004	2003
Computed expected tax	\$866,000	\$815,000	\$741,000
State income taxes, net of federal benefit	167,000	144,000	127,000
Stock options	(193,000)	(547,000)	(81,000)
Other	(60,000)	—	—
	\$780,000	\$412,000	\$787,000

At December 31, 2005, the Company had a net operating loss carryforward for federal income tax return purposes of approximately \$12,800,000 and for state purposes \$1,900,000 which expire between 2006 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,		
	2005	2004	2003
Beginning balance	\$2,315,000	\$1,731,000	\$1,448,000
Minority interest in GKF net income	1,126,000	983,000	928,000
Less: cash distributions	(912,000)	(399,000)	(645,000)
Minority interest	\$2,529,000	\$2,315,000	\$1,731,000

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NOTE 7—SHAREHOLDERS' EQUITY

1995 Stock Option Plan The Company's 1995 Stock Option Plan (the "1995 Plan") provided for nonqualified stock options and "incentive stock options." Under the 1995 Plan, 330,000 common shares were authorized for grant to officers and other key employees, non-employee directors, and advisors. The 1995 Plan terminated according to its terms on August 15, 2005. Provisions of the 1995 Plan included 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 stock option 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 received 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. There were approximately 140,000 options issued and exercisable as of December 31, 2005.

2001 Stock Option Plan The Company's 2001 Stock Option Plan (the "2001 Plan"), provides for nonqualified stock options and "incentive stock options." 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 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 stock option 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, 2005, approximately 7,000 stock options had been granted under the 2001 Plan.

Changes in options outstanding under the Stock Option Plans from January 1, 2003 to December 31, 2005 are as follows :

	Number of Options	Weighted Average Exercise Price
Balance at January 1, 2003	188,000	\$ 1.943
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	\$ 2.156
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	\$ 2.269
Granted	83,000	\$ 6.123
Exercised	(93,000)	\$ 1.665
Forfeited	(11,000)	\$ 4.065
Balance at December 31, 2005	147,000	\$ 5.029

The weighted average fair value of the options granted in 2005 was \$1.52.

American Shared Hospital Services

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 264,000, 846,000 and 125,000 options during 2005, 2004 and 2003 respectively. The exercise in 2005 resulted in a \$445,000 increase in paid in capital and a \$616,000 increase in deferred tax assets. The exercise in 2004 resulted in a \$994,000 increase to additional paid in capital and a \$1,540,000 increase in deferred tax assets, and in 2003 the exercise resulted in a \$163,000 increase to additional paid in capital and a \$244,000 increase in deferred tax assets. All options granted under the plan were exercised prior to the termination of the plan according to its terms on August 15, 2005.

The following table summarizes information about all options outstanding at December 31, 2005:

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
1.625-1.688	6,000	0.83	1.626	6,000	1.626
3.000-4.100	41,000	3.79	3.201	41,000	3.201
4.570-5.500	24,000	8.23	5.318	13,000	5.173
6.160-6.450	76,000	9.54	6.185	—	—
\$ 1.625-6.450	147,000	7.37	\$ 5.029	60,000	\$ 3.473

At December 31, 2005 and 2004, 60,000 and 411,000 options, respectively, were vested and exercisable. Automatic option awards 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. Discretionary options awarded during 2005 and 2004 vest over a five year period.

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 1995 and 2001 Plans was estimated assuming the following weighted-average assumptions:

	2005	2004	2003
Expected life (years)	10.0	10.0	10.0
Expected volatility	25.0%	37.0%	29.0%
Dividend yield	3.1%	3.0%	3.0%
Risk-free interest rate	4.3%	4.5%	4.3%

American Shared Hospital Services

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 have been no shares repurchased on the open market since the year ending December 31, 2001.

During 2005, the Company withheld 114,000 shares upon the exercise of options by two officers of the Company, to pay the exercise price of the shares and the withholding taxes associated with the exercises. The value of the exercise price is recorded as a reduction to common stock, and the difference between the exercise price and the market price at the time of exercise is recorded as a reduction to paid-in-capital.

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 December 2005 the Company declared dividends of \$0.0475 per share, payable in January 2006. In January, April, July and October of 2005 the Company paid dividends of \$0.045, \$0.045, \$0.0475 and \$0.0475 per share respectively. 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. The Company paid dividends of \$0.16 per share in the year ended December 31, 2003.

NOTE 8—RETIREMENT PLAN

The Company has a defined-contribution retirement plan (the “Plan”) that allows for a matching safe harbor contribution. For 2005, 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 \$35,000 to the Plan for the safe harbor match for each of the years ended December 31, 2004 and December 31, 2003, respectively. The Company has accrued \$44,000 for the estimated safe harbor matching contribution for the year ended December 31, 2005.

NOTE 9—OBLIGATIONS UNDER CAPITAL LEASES

During 2005 the Company entered into three capital lease obligations with three financing companies, collateralized by Gamma Knife equipment having an aggregate net book value of approximately \$4,518,000 at December 31, 2005. These obligations have stated interest rates ranging between 7.74% and 7.99%, are payable in 42 to 84 monthly installments, and mature between June 2009 and September 2012.

Future minimum lease payments, together with the present value of the net minimum lease payments under capital leases at December 31, 2005, are summarized as follows:

Year ending December 31,	Net Present Value of Minimum Lease Payments
2006	\$1,050,000
2007	1,050,000
2008	1,050,000
2009	762,000
2010	557,000
Thereafter	668,000
Total capital lease payments	5,137,000
Less imputed interest	939,000
	4,198,000
Less current portion	746,000
	\$3,452,000

American Shared Hospital Services

NOTE 10 – OPERATING LEASES

The Company leases office space and equipment under operating leases expiring at various dates through 2009.

Future minimum payments under noncancelable operating leases having initial terms of more than one year consisted of the following at December 31, 2005:

Year ending December 31,	
2006	\$ 208,000
2007	9,000
2008	9,000
2009	9,000
	<hr/>
	\$ 235,000

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 \$386,000, \$323,000, and \$315,000 for the years ended December 31, 2005, 2004 and 2003, 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.

NOTE 11 – COMMITMENTS AND CONTINGENCIES

Under the terms of existing Gamma Knife quotation agreements, the Company is committed to purchase upgrades and cobalt reloads to certain existing Gamma Knife equipment for \$2,109,000 when the equipment is upgraded at each customer location. At December 31, 2005, the Company had \$677,000 in deposits related to these purchase commitments which are classified as construction in progress.

NOTE 12 – MAJOR CUSTOMERS

Revenues from the Company's Gamma Knife segment were provided by twenty-one customers in 2005, eighteen customers in 2004, and seventeen customers in 2003. No individual customer exceeded 10% of the Company's total revenue in any of these years.

American Shared Hospital Services

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

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, 2005 and 2004, and the related consolidated statements of income, shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2005. 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. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. 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, 2005 and 2004, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2005 in conformity with U.S. generally accepted accounting principles.



San Francisco, California

March 29, 2006

American Shared Hospital Services

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, 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
March 31, 2005	\$6.23	\$5.40
June 30, 2005	\$6.28	\$5.23
September 30, 2005	\$6.17	\$5.71
December 31, 2005	\$7.35	\$5.80

The Company estimates that there were approximately 2,500 beneficial holders of its Common Shares at December 31, 2005.

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 in the open market 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 2005 holders of options to acquire the Company's common stock exercised their respective rights pursuant to such securities, resulting in the Company issuing 243,000 new shares of common stock for approximately \$68,000.

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, 2005 the Company had 5,018,885 issued and outstanding common shares, 396,530 common shares reserved for options, and 5,165 shares reserved pursuant to the Company's Shareholder Rights Plan.

In fourth quarter 2005, the Board of Directors declared a quarterly dividend of \$.0475 per common share to shareholders of record on January 3, 2006, paid on January 18, 2006. During 2005, shareholders of record as of January 3, 2005, April 4, 2005, July 1, 2005 and October 3, 2005 were paid quarterly dividends respectively as follows: \$.045 on January 14, 2005 and April 15, 2005, and \$.0475 on July 15, 2005 and October 17, 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: \$.04 on January 15, 2004 and April 16, 2004, \$.0425 on July 15, 2004 and \$.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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web: www.ashs.com

Registrar & Transfer Agent

American Stock Transfer &
Trust Company
59 Maiden Lane, Plaza Level
New York, NY 10038
Tel: 800.937.5449

Independent Registered Public Accounting Firm

Moss Adams LLP
Stockton, CA

Counsel

Davis Polk & Wardwell
Menlo Park, CA

Annual Shareholders' Meeting

June 28, 2006
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 Emeritus
Middlebury College
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 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, the risks of developing the Company's IMRT and The Operating Room for the 21st Century® programs, and the risks of investing in a development-stage company, Still River Systems, without a proven commercial product. 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 Company's filings with the Securities and Exchange Commission, including the Company's Annual Report on Form 10-K for the year ended December 31, 2005, and the definitive Proxy Statement for the Annual Meeting of Shareholders held on June 28, 2006.

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