

FINANCIAL INFORMATION

SELECTED CONSOLIDATED FINANCIAL DATA

CONSOLIDATED STATEMENTS OF OPERATIONS DATA (in thousands, except per share data):

YEAR ENDED DECEMBER 31,	2006	2005	2004	2003	2002
Product revenue	\$ 85,018	\$ 73,471	\$ 54,902	\$ 43,476	\$ 39,776
Strategic alliance revenue	6,316	3,524	662	615	—
Gross profit margin	69,163	57,692	42,572	33,193	27,961
Gross profit margin percentage	75.7%	74.9%	76.6%	75.3%	70.3%
Operating expenses:					
Research and development	15,280	10,464	7,470	7,287	7,827
Sales and marketing	35,571	30,298	26,695	25,241	28,449
General and administrative	12,446	10,291	8,946	7,833	7,942
Total operating expenses	<u>63,297</u>	<u>51,053</u>	<u>43,111</u>	<u>40,361</u>	<u>44,218</u>
Income (loss) from operations	5,866	6,639	(539)	(7,168)	(16,257)
Interest income, net	<u>3,332</u>	<u>1,926</u>	<u>923</u>	<u>725</u>	<u>956</u>
Income (loss) before taxes	9,198	8,565	384	(6,443)	(15,301)
(Benefit) provision for income taxes	(27,891)	90	81	80	—
Net income (loss)	<u>\$ 37,089</u>	<u>\$ 8,475</u>	<u>\$ 303</u>	<u>\$ (6,523)</u>	<u>\$ (15,301)</u>
Net income (loss) per share:					
Basic	\$ 1.66	\$ 0.39	\$ 0.02	\$ (0.34)	\$ (0.83)
Diluted	\$ 1.59	\$ 0.35	\$ 0.01	\$ (0.34)	\$ (0.83)
Weighted average shares used in computing net income (loss) per share:					
Basic	22,378	21,508	20,142	19,413	18,450
Diluted	23,380	23,921	22,286	19,413	18,450

CONSOLIDATED BALANCE SHEET DATA (in thousands):

AS OF DECEMBER 31,	2006	2005	2004	2003	2002
Cash, cash equivalents, restricted cash and marketable securities	\$ 63,470	\$ 43,773	\$ 32,295	\$ 31,162	\$ 36,865
Working capital	67,380	47,988	34,224	30,680	36,734
Total assets	124,964	87,132	61,690	47,740	54,480
Long-term debt	—	—	186	525	1,015
Total stockholders' equity	109,248	67,423	45,586	30,968	36,797

These selected condensed financial statements should be read in conjunction with the full audited financial statements presented in Aspect's Form 10-K, as filed with the Securities and Exchange Commission.

CORPORATE INFORMATION

Annual Meeting of Stockholders

All stockholders are welcome to attend our annual meeting, which will be held at 9:00 am on Wednesday, May 23, 2007, at Aspect Medical Systems, Inc., One Upland Road, Norwood, Massachusetts. We look forward to meeting our stockholders and answering any questions you may have at the meeting.

Forward-Looking Statements

Certain statements made in this Annual Report to Stockholders are forward-looking statements that are subject to risks and uncertainties, including statements regarding the Company's near-term and long-term operating plans, strategies and goals. There are a number of important factors that could cause the Company's future performance and results of operations to differ materially from such statements, including without limitation those set forth under the heading, "Risk Factors" in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2006, which is filed with the Securities and Exchange Commission. These statements should not be relied upon as representing the Company's expectations or beliefs as of any date subsequent to the date of this Annual Report.



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Chairman of the Board of Directors

Boudewijn Bollen
President of International Operations

Michael Esposito
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Stanford University

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Boudewijn Bollen
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John Coolidge
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Vice President of Engineering

Philip H. Devlin
Vice President and General
Manager of Neuroscience

William Floyd
Vice President of Sales and Marketing

Scott D. Kelley, M.D.
Vice President of Medical Affairs

Paul J. Manberg, Ph.D.
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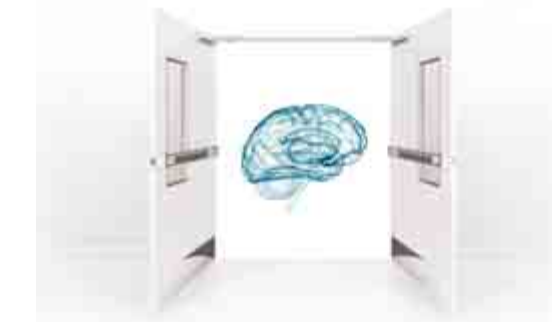
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Form 10-K

The Company's Annual Report on Form 10-K, as filed with the Securities and Exchange Commission for the fiscal year ended December 31, 2006, is available free of charge upon written request to Aspect Medical Systems, Inc., Investor Relations Department, One Upland Road, Norwood, Massachusetts 02062.



ANNUAL REPORT 2006

Dear Stockholders:

When we introduced our first BIS™ monitor in 1996, brain monitoring was a new concept that required a significant change in anesthesia practice. Today, Aspect is reporting \$91 million in annual revenues and brain monitoring is widely used to guide anesthesia care in healthcare facilities throughout the United States and across the globe. The clinical evidence supporting the reliability of BIS technology and its safety and quality benefits has continued to grow, and brain monitoring is moving closer to becoming a standard component of anesthesia and sedation care.

Our efforts to date have established the BIS brand as the quality and performance leader in consciousness monitoring and we intend to maintain our commitment to research and innovation to retain this leadership position. Moreover, we intend to build upon the BIS brand with new brain assessment technologies in substantial new markets.

Although our revenue growth slowed, 2006 was a strong year for Aspect in many respects:

- Worldwide product revenue increased by 16%
- Our installed base grew 24% to nearly 40,000 units worldwide

In 2006, the American Society of Anesthesiologists (ASA) published a Practice Advisory on intraoperative awareness. This document formally acknowledged awareness as an important clinical problem and suggested that anesthesiologists carefully consider the use of brain function monitoring as a tool to assist them in avoiding awareness. Outside the United States, two prominent anesthesia societies issued similar guidance: the Australian and New Zealand College of Anesthesiologists and the Madrid Centro Society for Anesthesia. Further, several prominent hospitals and hospital networks in the U.S., including the Cleveland Clinic Foundation, launched comprehensive patient safety programs to reduce the incidence of patient awareness during anesthesia and made BIS monitors widely available to encourage brain monitoring in patients at risk.

This activity has resulted in increased availability of brain monitoring technologies at hospitals across the globe. Today, BIS monitoring is available in 53% of all operating rooms in the U.S. and has been used on approximately 19 million patients worldwide. Nonetheless, we believe that the untapped market opportunity remains substantial. Penetrating the remaining market represents Aspect's next big challenge, as it includes many "later adopters" of new technology. Yet we are confident that we can make meaningful inroads into this untapped market.

Our optimism is partially rooted in an analysis of our existing customer base. Within our top 150 customers in the U.S., we estimate that BIS is now used in 75% of all procedures that involve deep sedation or general anesthesia. Within our top 600 customer accounts, which perform approximately 25% of all surgeries in the country, we estimate that BIS is used in 48% of all cases. In contrast, an analysis of all U.S. hospitals performing general anesthesia shows that BIS is used in only 16% of all eligible procedures. Aspect's challenge is to bring average utilization of BIS monitoring up to the levels seen among our best customers. We have demonstrated that we can achieve these rates of use among a large subset of



hospitals, including many of the nation's largest and best hospitals whose practices heavily influence standards of care at the local and regional level.

Many of our current customers adopted BIS technology because they value our product for its role in helping them reduce the risk of awareness or for the precision with which it allows them to administer anesthesia. To increase utilization of our technology and reach the next tier of the market, we are working to develop expanded product offerings and resources to provide both clinicians and hospital administrators with new reasons to incorporate BIS monitoring. To achieve this objective we have established several strategies.

EXPANDED PRODUCT OFFERINGS AND EDUCATION RESOURCES

Near term, we'll focus on continued expansion of BIS product offerings. We now offer customers greater choice in BIS products, including BIS VISTA™, a higher-end, advanced stand-alone monitor; as well as an array of BIS modules that are compatible with multi-parameter monitoring equipment made by our OEM partners. BIS technology remains the only consciousness monitoring solution that has been integrated into the patient monitoring systems of the world's leading manufacturers of monitoring equipment, including Datex-Ohmeda, Datascope, Dixtal, Draeger Medical, GE Healthcare, Nihon Kohden, Mindray, Philips Medical and Spacelabs Medical. Taken together, our stand alone products and those integrated into other monitoring equipment give customers a wide variety of BIS solutions to choose from to address a range of economic and clinical requirements.

To ensure that anesthesia providers achieve meaningful benefits from their investment in our products, we plan to continue to expand our recently launched BIS EPIC (Education Programs for Improved Care) offering, a major continuing education initiative that provides a portfolio of educational resources (onsite training, lectures and web-based e-learning tools among them) that can be customized to enhance customer understanding of how BIS can be used to achieve anesthesia goals. In our past experience, an investment in training and education has had a positive impact on utilization of BIS to improve patient care.

Another key element of our short-term strategy to increase market penetration is to focus our resources selling to integrated delivery networks, or IDNs. Today, many hospitals that comprise the remaining untapped market are members of an IDN where purchasing and policy decisions are set at the network level. Thus, we believe that targeting these IDNs is a cost-effective way to reach deeper into the market.

PRODUCT ENHANCEMENTS AND ANESTHESIA OUTCOMES RESEARCH

Looking a little further out on the horizon, within the next three to five years Aspect is planning a number of anesthesia outcomes research initiatives that we believe further expand the proven value and benefits associated with BIS monitoring.

First, we plan to continue to build on research presented at last year's ASA meeting that examined fluctuations in BIS values and facial electromyogram, or EMG. Early research suggests that fluctuations in BIS and EMG values during surgery may be associated with intraoperative arousal and post-operative pain. We are now exploring ways to quantify and display this information with the goal of developing more advanced monitoring capabilities on our BIS systems that will help anesthesia professionals maximize patient comfort by tracking intraoperative analgesic requirements and reducing post operative pain.

Second, we plan to focus on expanding our clinical research program in an effort to document the value of BIS monitoring on longer-term patient outcomes. Several recent studies have led to growing interest in the medical community to better understand the potential long-term adverse consequences associated with excessive anesthesia exposure, particularly of inhaled anesthetics. These studies suggest that a range of negative outcomes, including seizures, delirium, post-operative cognitive dysfunction, inflammatory response, cancer recurrence and even mortality, may be associated with overexposure to anesthetic agents - with young children and the elderly possibly at greatest risk. Doctors are calling for more research and the U.S. Food and Drug Administration recently convened a panel to address concerns about potential neurodegenerative effects of anesthetics in pediatric patients.

As part of this initiative, Aspect is conducting neuromonitoring research on anesthesia outcomes in children and adults, and we expect to initiate several new studies this year. We recently announced the initiation of two studies being conducted with the Cleveland Clinic. The first study is designed to examine if a variety of anesthetic management techniques, including avoidance of deep anesthesia, improve outcomes in patients undergoing major vascular surgery. In the second, we plan to test the hypothesis that avoiding deep general anesthesia reduces cancer recurrence rates in women undergoing surgery for breast cancer. In 2007, we also intend to initiate research to assess the benefits of BIS-guided care in critical care and procedural sedation settings.

Although the final results from these studies may not be available for two to three years, important interim results focusing on process improvements, complications requiring interventions in the recovery room, delirium and post operative cognitive dysfunction are expected to be reported earlier. We anticipate that this growing body of research may help further define the role of BIS monitoring in helping clinicians control depth of anesthesia and sedation to improve the safety and quality of patient care.

Third, we believe that by continuing to demonstrate improved outcomes associated with BIS monitoring we will be better able to help our customers meet "pay for performance" standards that are emerging in the U.S. and parts of Europe. The pay for performance approach ties clinician payment to measurable benchmarks of quality and safety outcomes that we believe BIS monitoring can help them achieve.

NEUROSCIENCE INITIATIVES IN DEPRESSION AND ALZHEIMER'S DISEASE

Long term, we continue to be very excited by the potential opportunities for new product development as a result of our neuroscience research in depression and Alzheimer's disease.

In depression, our primary investigative effort continues to be focused on identifying biomarkers that will guide clinicians in selecting effective pharmacological treatments for the millions of people worldwide who suffer from depression. In the U.S. alone, more than 15 million people experience a major depressive episode every year and 17% of all adults experience major depression in their lifetimes. Those who suffer with this condition know that it typically takes weeks before the efficacy of a specific anti-depressant can be determined and that patients may undergo several trial and error drug regimes before finding relief.

In collaboration with leading researchers at ten academic centers across the United States, our BRITE Major Depression study ("Biomarkers for Rapid Identification of Treatment Efficacy") is designed to help Aspect develop brain assessment technology to help predict an individual's response to antidepressant treatment and help physicians more quickly prescribe medicine most likely to provide relief. Interim results from the trial produced significant data that we plan to present at clinical meetings in the second quarter of 2007. We expect that analysis of the full data from this study will be complete later this year; which will help guide our clinical, regulatory and commercialization strategies in this area.

Although our technology holds promise to help guide pharmaceutical-based treatments for depression, existing treatment options for depression leave many patients with significant illness. Accordingly, we also plan to explore the role of brain monitoring in optimizing device-based therapies – particularly neurostimulation approaches - for depression and other neuro-psychiatric conditions.

Similarly, our research on cognitive dysfunction and the opportunity to improve the quality of life for patients suffering from dementia and Alzheimer's disease is significant. Four and a half million Americans suffer from Alzheimer's and 400,000 new cases are diagnosed every year. Alarming, dementia in all its forms is increasingly afflicting people in their 40s, 50s and 60s, so it is no longer solely a disease of the elderly.

Aspect is involved in two studies that are providing the data we need to strengthen our understanding of early neurophysiological markers of cognitive function. Promising new therapies for Alzheimer's and other forms of dementia are on the horizon, and we hope that our research and product development efforts will lead to new brain monitoring technologies designed to increase treatment effectiveness through early diagnosis.

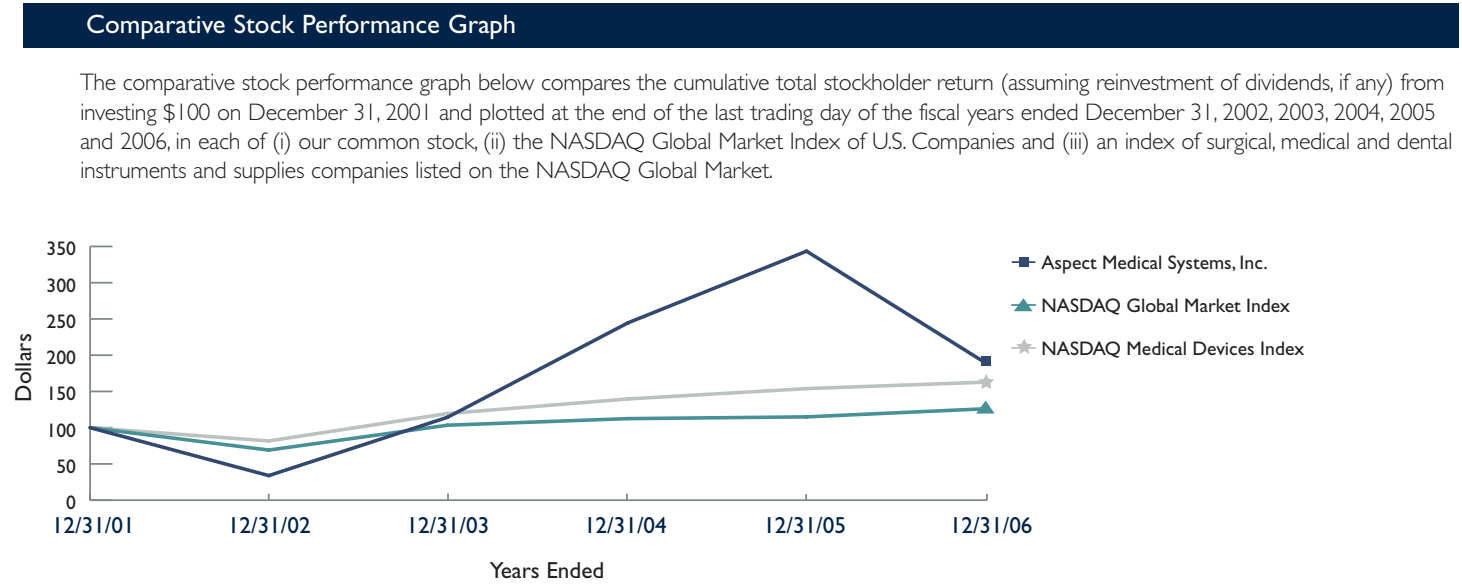
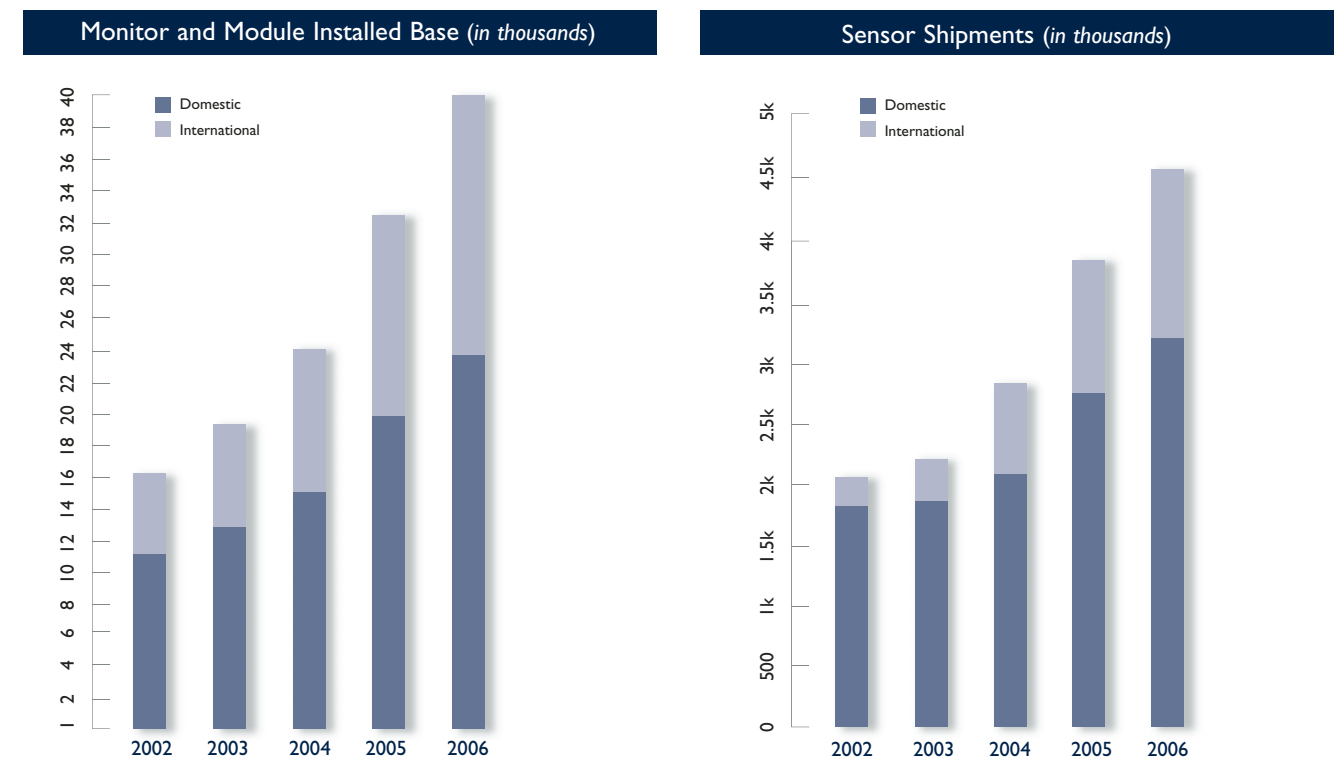
IN CONCLUSION

In 2006, we successfully managed a program of disciplined expense control and increased profitability during a period of slowed growth. We accomplished this while moving into a new corporate headquarters in Norwood, Massachusetts that we believe will enable us to sustain our future growth. Over the years we have built an exceptional team composed of people with tremendous experience in brain monitoring, a strong work ethic and most importantly, a strong commitment to improving the quality of care and quality of life for patients through innovative brain monitoring technologies. I believe that this team will continue to develop and gain acceptance of these innovative technologies with a goal of creating long-term value for our shareholders. I'm looking forward to the road ahead, and thank you for your continued support.

Sincerely,



Nassib G. Chamoun
President, CEO and Founder



Measurement Period (Fiscal Year Covered)	Aspect Medical Systems, Inc.	NASDAQ Global Market Index	NASDAQ Medical Devices Index
12/31/01	\$ 100.00	\$ 100.00	\$ 100.00
12/31/02	\$ 33.90	\$ 69.10	\$ 81.70
12/31/03	\$ 114.30	\$ 103.40	\$ 119.50
12/31/04	\$ 244.60	\$ 112.50	\$ 139.60
12/31/05	\$ 343.50	\$ 114.90	\$ 153.90
12/31/06	\$ 188.10	\$ 126.20	\$ 162.90

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