U.S. SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-KSB

[X] ANNUAL REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

FOR THE FISCAL YEAR ENDED DECEMBER 31, 1997

[ ] TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

FOR THE TRANSITION PERIOD FROM _____ TO _____

COMMISSION FILE NUMBER 1-12471

INTEGRATED SURGICAL SYSTEMS, INC.
(NAME OF SMALL BUSINESS ISSUER IN ITS CHARTER)

DELAWARE	68-0232575
(STATE OR OTHER JURISDICTION OF INCORPORATION OR ORGANIZATION)	(I.R.S. EMPLOYER IDENTIFICATION NO.)
829 WEST STADIUM LANE, SACRAMENTO, CA	95834
(ADDRESS OF PRINCIPAL EXECUTIVE OFFICES)	(ZIP CODE)

(916) 646-3487
(ISSUER'S TELEPHONE NUMBER, INCLUDING AREA CODE)

SECURITIES REGISTERED UNDER SECTION 12(b) OF THE EXCHANGE ACT:

TITLE OF EACH CLASS	NAME OF EACH EXCHANGE ON WHICH EACH CLASS IS REGISTERED
COMMON STOCK, $.01 PAR VALUE	THE PACIFIC EXCHANGE INCORPORATED
COMMON STOCK PURCHASE WARRANTS	THE PACIFIC EXCHANGE INCORPORATED

SECURITIES REGISTERED UNDER SECTION 12(g) OF THE ACT:
NOT APPLICABLE
(TITLE OF CLASS)

Check whether the issuer: (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.
Yes [X] No [ ]

Check if there is no disclosure of delinquent filers in response to Item 405 of Regulation S-B contained in this form, and no disclosure will be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-KSB or any amendment to this Form 10-KSB. [ ]

Revenues for the issuer's most recent fiscal year were $4,933,824

The aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the closing price of the common stock on March 6, 1998 was $20,500,000.

ISSUERS INVOLVED IN BANKRUPTCY PROCEEDINGS
DURING THE PAST FIVE YEARS

Check whether the issuer has filed all documents and reports required to be filed by Section 12, 13 or 15(d) of the Exchange Act after the distribution of securities under a plan confirmed by a court. Yes [ ] No [ ]

APPLICABLE ONLY TO CORPORATE REGISTRANTS

As of March 6, 1998, the issuer had 5,503,390 shares of common stock, $.01 par value, outstanding.

Transitional Small Business Disclosure Format: Yes [ ] No [X]

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's definitive Proxy Statement for its 1998 Annual Meeting of Stockholders are incorporated by reference into Part III of this Form 10-KSB in response to Items 9, 10, 11 and 12 of Part III.

PART I

ITEM 1. DESCRIPTION OF BUSINESS.

Integrated Surgical Systems, Inc. (the "Company") develops, assembles, markets and services image-directed, computer-controlled robotic products for orthopaedic and neurological applications. The Company was incorporated under the laws of the State of Delaware on October 1, 1990.

Orthopaedic Business

The Company's principal orthopaedic product is the ROBODOC(R) Surgical Assistant System (the "ROBODOC System"), consisting of a computer-controlled surgical robot and the Company's ORTHODOC(R) Presurgical Planner (the "ORTHODOC"). The ROBODOC System has been used for primary total hip replacement surgery on over 2,000 patients in Europe. The Company believes its "active" robotic system is the only available system that can accurately perform key segments of surgical procedures with precise tolerances generally not attainable by traditional manual surgical techniques. The ROBODOC System also allows the surgeon to prepare a preoperative plan specifically designed for the characteristics of the individual patient's anatomy. The technology for the ROBODOC System was initially developed at the University of California, Davis, in collaboration with International Business Machines Corporation ("IBM").

The ROBODOC System cannot be marketed in the United States until clearance or approval is obtained from the U.S. Food and Drug Administration (the "FDA"). As a result of a recent pre-filing meeting with representatives of the FDA, the Company intends to file a premarket approval application ("PMA") with the FDA in the second quarter of 1998 for approval to market the ROBODOC System in the United States. There can be no assurance as to when or if the FDA will grant PMA approval to the ROBODOC System.

The ORTHODOC is a computer workstation that utilizes the Company's proprietary software for preoperative surgical planning. The ORTHODOC is a part of the ROBODOC System, but the Company also plans to market it separately. The Company commenced marketing the ORTHODOC in the United States in the first quarter of 1998. The ORTHODOC received 510(k) clearance from the FDA for marketing in the United States on a stand-alone basis in January 1997. The ORTHODOC converts CT scan data of a patient's femur into three-dimensional images, and through a graphical user interface, allows the surgeon to examine the bone more thoroughly and to select the optimal implant for the patient using a built-in library of available implants. A tape of the planned surgical procedure, developed by the ORTHODOC, guides the surgical robot arm of the ROBODOC System to accurately mill a cavity in the bone, thus allowing the surgeon to properly orient and align the implant. Prior to the primary surgery, two titanium locator pins are placed in the patient's femur in an outpatient procedure. These locator pins are used during the primary procedure to orient the ROBODOC System to the ORTHODOC preoperative plan. Non-clinical scientific data published by scientists from the Company and IBM demonstrate that as a result of the precise milling of a cavity, the ROBODOC System achieves over 95% bone-to-implant contact, as compared to an average of 20% bone-to-implant contact when surgery is performed manually.

THR surgery involves the insertion of an implant into a cavity created in the patient's femur. The Company believes that precise fit and correct alignment of the implant within the femoral cavity are key factors in the long-term success of THR surgery. In conventional THR surgery, a bone cavity is cut in the shape of the implant manually with metal tools, and the surgical plan, including the selection of the size and shape of the implant, is generally formulated based upon patient data obtained from two-dimensional x-ray images of the patient's femur. Based upon clinical experience to date in Europe with the ROBODOC System, patients generally have become weight-bearing in a shorter period than generally experienced by patients who have had this surgery performed manually. In addition, clinical data obtained from trials in Europe and the United States indicates that intraoperative fractures have been dramatically reduced in the THR surgeries performed with the ROBODOC System (no intraoperative fractures have resulted from THR surgeries performed with the ROBODOC System to date). The Company also believes fewer hip revision surgeries

(implant replacements) may be necessary for patients who have had primary THR surgery performed with the ROBODOC System, as compared to patients who have this surgery performed manually.

In the past, a majority of THR implants have been held in place with acrylic cement, which fills the spaces between the implant and the bone, thereby anchoring the implant to the femoral cavity ("cemented implants"). During the 1980s, implants that did not require cement ("cementless implants") were developed with materials designed to stimulate bone ingrowth. The selection of a cemented or cementless implant generally is based upon a patient's bone condition and structure, age and activity level. Typically, cemented implants are used for older, less active patients. Furthermore, most implants require replacement within five to 20 years of the first operation in collaboration with IBM and Johns Hopkins University. The Company has developed a software package for hip revision surgery that eliminates the distortion of the x-ray images of the patient's femur used in planning hip revision surgery caused by the metal in the existing implant. A surgeon using this software will have a clearer view of the remaining bone in planning hip revision surgery and therefore will be better able to remove fragmented cement without removing any of the remaining thin thigh bone. The Company commenced marketing the software package for the hip revision application to its customers in Europe in the first quarter of 1998.

Neurosurgical Business

The Company entered the neurosurgical business through the acquisition of Innovative Medical Machines International, S.A. ("IMMI") on September 5, 1997. IMMI's principal neurosurgical product is the NeuroMate System, consisting of an image-guided, computer-controlled robotic arm, head stabilizer and monitor. The Company also offers a workstation with presurgical planning software through arrangements with original equipment manufacturers ("OEMs").

The NeuroMate System has been used to perform over 1,500 neurosurgical procedures in France and Japan. The Company believes that the NeuroMate System, which uses IMMI's proprietary robotic arm design and control systems designed specifically for use in the operating room, is the only image-guided, computer-controlled robot currently in use to precisely position and hold critical tools used in the performance of neurosurgical procedures. The Company commenced marketing the NeuroMate System in the United States in the fourth quarter of 1997. The NeuroMate System received 510(k) clearance from the FDA for marketing in the United States in May 1997.

Stereotactic neurosurgery is a minimally invasive approach to operating on the brain. Because the brain is largely unexposed, it requires the surgeon to work without direct visualization of the brain itself. This is overcome by a thorough understanding of brain anatomy and by using a spatial coordinate system that allows the surgeon to "navigate" within the brain without directly visualizing it. Essentially, the coordinate space of the patient's brain is correlated to the patient's own CT, magnetic resonance (MR) or other images by using anatomical landmarks that are shared by the patient and the images. This is known as "registration" of the patient's coordinate space to the coordinate space of the images. Once this is accomplished, the patient's CT scan can be used to guide the surgeon to specific sites within the brain through small holes the surgeon has made in the cranium (i.e., not necessitating a craniotomy).

POTENTIAL ORTHOPAEDIC AND NEUROSURGICAL APPLICATIONS

The Company intends to offer separate software packages for each new application if, as and when developed by the Company. Consequently, the Company's customers would be able to use the Systems as platforms to perform a variety of surgical procedures without incurring significant additional hardware costs. The Company plans to develop software packages for the following orthopaedic and neurosurgical surgical procedures.

- - Potential Orthopaedic Applications

Hip Revision. Hip revision surgery generally is required to replace loose or otherwise failed implants. Most implants require replacement in five to 20 years after the first operation. Hip revision surgery generally is difficult, time consuming and complex. The metal in the existing implant distorts x-ray images used for

planning the surgery, obstructing the view of the remaining bone and, if a cemented implant is to be replaced, the location of the cement mantle. The removal of the fragmented cement without removing any of the remaining thin bone structure is a major challenge for the surgeon.

The Company has developed a software package for hip revision surgery using the ROBODOC System, in collaboration with IBM and Johns Hopkins University. The development of the hip revision application has been funded in part by a grant from the National Institute for Standards and Technology (Advanced Technology Program) of the United States Department of Commerce. The first phase of the hip revision project related to the development and implementation of software to create a clearer image of the remaining bone and fragmented cement in preparing the surgical plan. The second phase of the project involved its validation in a clinical setting. The Company believes that its hip revision software will improve surgical planning and enable the robot to remove cement more precisely than if the hip revision procedure were performed manually. The Company commenced marketing the software package for the hip revision application to its customers in Europe in early 1998.

Total Knee Replacement. The Company plans to develop a software package for total knee replacement ("TKR") surgery using the ROBODOC System. The proposed application module is intended to enable the ROBODOC System to select the optimal implant for the patient and make accurate cuts in the bone, thus allowing the surgeon to properly orient and align the implant. The proposed application module to be developed by the Company for TKR surgery performed with the ROBODOC System, if and when developed, is intended to result in a precise and accurate fit for implants that are properly sized and placed, regardless of bone quality. Furthermore, the Company believes that if and when this application module is developed, implant longevity and the prognosis for restored biomechanics will be significantly improved as a result of TKR surgery performed with the ROBODOC System.

Acetabulum Replacement and Revision. The Company plans to complement the THR femoral replacement application with acetabular cup planning and bone preparation for hip socket replacement surgery. Currently, surgeons estimate the size of the cup-shaped cavity in hip socket surgery using x-rays, which are subject to distortion. Working in a narrow space with a limited view, the surgeon ultimately selects the final cup size through trial and error. Due to the limitations of available surgical tools, the surgeon is obliged to use a hemispheric reamer and cup, although the human acetabulum (hip socket) is an irregular shape. The Company believes that the application module for this application, if and when developed, would enable the computer-controlled robot to prepare an accurate bed for the implant, based on its specifications, and could prepare an irregularly shaped socket for a custom or anatomically-shaped acetabular component. The three-dimensional capability of the ORTHODOC would better enable it to determine and display the irregular shape of the acetabulum and instruct the robot to prepare the proper socket. This procedure potentially could solve the problem of leg-length discrepancies which often originate at the acetabulum.

Osteotomies. Osteotomies are precise cuts in bone intended to reshape or realign abnormal or deformed structures. The Company's engineers have generated a detailed work plan to adapt the ROBODOC System for use in performing long-bone osteotomies on femurs and tibias (i.e., shin bones). The proposed application module for this application, if and when developed, is intended to enable the surgeon using the views of the bone created by the ORTHODOC from CT scan data, to make trial cuts, remove bone and manipulate the remaining fragments, and experiment with the appropriate placement of plates and screws. The surgeon's final plan would be saved on a tape that would instruct the robot where to make saw cuts. The computer-controlled robot would then orient itself in space by using topographical features of the operative bone. A fixator would secure the bone to the robot. The computer-controlled robot would then pre-place screw holes to facilitate the final realignment and make the actual cuts.

- - Potential Neurosurgical Applications

Spine surgery. Surgical interventions in the spine generally involve tumor biopsy/resection; vascular repair; implants of plates, rods, screws, or other implantable devices or substances; and bone fusions of various types. The Company believes that its image-directed, computer-controlled robotic technology is applicable in most of these interventions and will significantly enhance precision and accuracy in many of them. Spine surgery is a large segment of both neurosurgery and orthopaedic surgery, as the nature of the abnormality may

involve the nervous system or the vertebral column, or both. A significant part of this application involves the insertion of vertebral pedicle screws, discussed below.

Vertebral Pedicle Screws. Pedicle screws are used to fuse vertebrae in need of repair due to trauma or herniated disc disease. The procedure involves the placement of screws straight down the center of an irregular section of a fragile bone only twice the diameter of the screw itself. Precise placement of a screw affects the outcome of the surgery. Misplacement of a screw can result in failure of the repair, trauma to the adjacent spinal cord, or rupture of nearby blood sinuses which can hemorrhage severely. The Company believes that if and when the development of the proposed application module for this surgical procedure is completed, the NeuroMate System will be capable of performing this surgical procedure more safely and effectively than surgery performed manually since the computer-controlled robot is better able to precisely orient its tool in a manner compatible with what is required for screw placement.

MARKETING, SALES AND DISTRIBUTION

The ROBODOC System cannot be marketed in the United States until clearance or approval is obtained from the FDA. The Company has received 510(k) clearance from the FDA to sell the ORTHODOC in the United States. The NeuroMate System also has received 510(k) clearance from the FDA for marketing in the United States and from the Japanese Ministry of Health for marketing in Japan. Presentations to potential customers focus on the clinical benefits obtained by patients, and the potential financial and marketing benefits obtained by hospitals and surgeons.

The Company has commenced marketing the ROBODOC System to orthopaedic and trauma surgeons and hospitals in Europe through direct sales and arrangements with implant manufacturers. To date, the Company's direct sales efforts have been primarily in Germany and Austria. Over 1,000 THR surgeries have been performed with the ROBODOC Systems at the Berufsgenossenschaftliche Unfallklinik ("BGU") clinic in Frankfurt, Germany since August 1994. As result of a significant increase in the number of THR surgeries performed at the clinic with the ROBODOC System, the BGU clinic purchased a second ROBODOC System in the second quarter of 1996. The Company commenced marketing the ORTHODOC to hospitals, orthopaedic surgeons and implant manufacturers in the United States in the first quarter of 1998.

The NeuroMate System is being marketed in Europe through a direct sales force, in Japan through a Japanese distributor, and in the United States through a direct sales force and select distributors.

The Company promotes its products through presentations at trade shows and advertisements in professional journals and technical and clinical publications, as well as through direct mail campaigns. To accelerate sales and reduce the lengthy sales cycle, the Company has entered into informal leasing arrangements with two major multinational leasing companies.

MANUFACTURING

The Company's production process consists primarily of final assembly of purchased components, testing of the products and packaging, and is conducted at its facilities in Sacramento, California and Lyon, France. The Company purchases substantially all the components for its Systems from outside vendors, then assembles these parts and installs its proprietary software.

The ROBODOC System consists of the robot, base and the control cabinet, which are connected through four interface cables, and the ORTHODOC. The NeuroMate System consists of a robot arm, electronics control and base. Sankyo Seiki of Japan supplies the robot for the ROBODOC System customized to the Company's specifications and Audemars-Piguet supplies the customized robot for the NeuroMate System. Upon delivery of a robot, the Company performs a series of tests to verify proper functioning. The customization and supply process for the robots currently requires approximately four months lead time. While the robots can be obtained from other suppliers with appropriate modifications and engineering effort, there can be no assurance that delays resulting from the required modifications or engineering effort to adopt alternative components would not adversely affect the Company. Ancillary items required to perform robotic

surgeries, including devices for fixing the hip and attaching it to the robot, numerous probes, cutter bearing sleeves and tool guides, are assembled and tested separately.

Consumables, including sterile drapes, bone screws, cutters and pendants, are also manufactured by outside vendors according to the Company's specification and are inspected upon receipt to ensure that these specifications are consistently met. The Company purchases these items in quantity and distributes them on a per order basis. The Company also coordinates the packaging and sterilization of certain items. The Company's policy is to procure its consumables from vendors that it approves after ensuring that the goods comply with the Company's sterilization requirements.

The ORTHODOC consists of a pentium-based computer workstation and associated peripherals, and includes the Company's proprietary software. The Company purchases and then tests the computer as a complete package. A computer board is added to interface to CT/x-ray scanner input modules and, if required, the ROBODOC System's tape output drive. The hard drive is reformatted to accept the operating system, and appropriate ORTHODOC software is installed. The unit is built configured for 110 or 220 AC volt operation.

The Company's production facilities are subject to periodic inspection by the FDA for compliance with Good Manufacturing Practices ("GMP"). In addition, the Company's products will be required to satisfy European manufacturing standards for sale in Europe. The Company believes that it is in compliance with GMP and expects to obtain ISO-9000 certification prior to June 14, 1998, the date after which such certification will be required for sales of its products in Europe.

RESEARCH AND DEVELOPMENT

Since its inception, the Company's research and development activities have focused on the development of innovative image-directed computer-controlled robotic products for surgical applications and operating software for these products. The Company incurred research and development expenses of approximately $2,469,000 and $3,064,000 in connection with the development of the ROBODOC System and the ORTHODOC for the years ended December 31, 1996 and December 31, 1997, respectively.

The Company has developed a software package for hip revision surgery, in collaboration with IBM and Johns Hopkins University, funded in part by a grant from the National Institute for Standards and Technology (Advanced Technology Program) of the United States Department of Commerce ("NIST"). Hip revision surgery generally is difficult, time consuming and complex. The metal in the existing implant distorts x-ray images used for planning the surgery, obstructing the remaining bone and, if a cemented implant is to be replaced, the location of the cement mantle. The removal of the cement mantle without removing any of the remaining thin bone structure is a major challenge for the surgeon. The first phase of the hip revision project related to the development and implementation of software to create a clearer image of the remaining bone and fragmented cement in preparing the surgical plan. The second phase of the project involved its validation in a clinical setting. The Company believes that its hip revision application module will improve surgical planning for hip revision surgery and enable the robot to remove cement more precisely than if the hip revision procedure were performed manually.

Under the terms of the NIST grant, the Company, IBM and Johns Hopkins University are entitled to reimbursement for 49% of the expenses incurred in connection with the project for a period of three years. The maximum amount of expenses subject to reimbursement under the grant is approximately $4,000,000, so that not more than $1,960,000 in expenses may be reimbursed in the aggregate to the Company, IBM and Johns Hopkins University under the grant. The Company has incurred research and development expenses of approximately $991,000 in connection with the hip revision project through December 31, 1997. As of December 31, 1997, the Company had received $452,000 under the terms of the grant. The Company commenced marketing the software for the hip revision application to its customers in Europe in the first quarter of 1998.

The Company offers five lines of prostheses in its software library of hip implants on its ORTHODOC. It is expanding the library to include multiple implant lines, revision stems, and custom-made prostheses. The

Company has received orders from Howmedica, a division of Pfizer, and Johnson & Johnson Professional, Inc. ("J&J") to add their respective hip prostheses to its existing software library, which included the implant libraries of Biomet and DePuy. When completed, this will allow orthopaedic surgeons to plan hip replacement surgeries using Howmedica's and J&J's line of implants. The Company will further expand the library of implants used at clinical sites to include multiple implant lines, revision stems, and custom-made prostheses. The Company has also commenced preliminary work with respect to the application of the base technology for total knee replacement and with respect to the application of the base technology for total knee replacement surgery.

IMMI is the recipient of an interest-free loan from ANVAR (a national agency in France established to aid research and development projects) in the amount of approximately $143,000 as of December 31, 1997. This loan provides funding for the development of the NeuroMate System for spine surgery. This project is currently in its first phase of development in connection with a University hospital in Lille, France. Under certain conditions (e.g., if at the completion of the project it is not deemed a "success") there will be no requirement to repay the loan.

IMMI also is the recipient of a grant from ANVAR in the amount of approximately $174,000, all of which IMMI had received as of December 31, 1997. This grant funds 50% of the cost to build and install NeuroMate Systems at two clinics in France as well as the costs to perform a clinical study at these sites.

COMPETITION

The principal competition for the ROBODOC System is manual surgery performed by orthopaedic surgeons, using surgical power tools and manual devices. The providers of these instruments are the major orthopaedic companies, which include Howmedica, Inc. (a subsidiary of Pfizer, Inc.), located in New York; Zimmer, Inc. (a subsidiary of Bristol-Myers Squibb Company), located in Indiana; Johnson & Johnson Orthopaedics, Inc. (a subsidiary of Johnson & Johnson), located in New Jersey; DePuy, Inc., located in Indiana; Biomet, Inc. located in Indiana; and Osteonics, Inc. (a subsidiary of the Stryker Corporation), located in New Jersey. MAQUET, a manufacturer of operating tables located in Germany, has announced that it intends to market a device similar to ROBODOC in mid 1998. The principal competition for the NeuroMate System is from manufacturers of frame-based and frameless stereotactic systems, some of which are commonly called "navigators". Approximately twenty navigator models have been introduced, including those by Radionics, Sofamor Danek, and Ohio Medical Surgical Products, all located in the U.S.; Elekta, located in Sweden; and, Fischer Leibingher and Brain Lab, both located in Germany. In addition, there are companies in the medical products industry capable of developing and marketing computer-controlled robotic systems for surgical applications, many of whom have significantly greater financial, technical, manufacturing, marketing and distribution resources than those of the Company, and have established reputations in the medical device industry. However, the Company believes that it enjoys a significant competitive advantage over such companies in view of the time required to develop an image-directed, computer controlled robotic system and to obtain the necessary regulatory approvals, including the sponsorship of clinical trials. There can be no assurance that future competition will not have a material adverse effect on the Company's business.

The Company's ROBODOC System represents a significant technological advancement with respect to the manner in which THR surgery is performed. The Company's image-directed, computer-controlled robotic technology is intended to complement, rather than replace, surgeons in performing THR and other orthopaedic surgeries. Although there are companies which market technologically advanced surgical tools used by surgeons in performing orthopaedic surgeries, including passive robot systems that direct the surgeon in planning and performing surgical procedures (e.g., aiming and holding devices), the Company believes that the ROBODOC System is the only active robotic system that performs a key segment of THR surgery (i.e., milling a bone cavity) under the supervision of a surgeon.

The Company believes the NeuroMate System is the only robotic system presently used for neurosurgery which provides superior accuracy and flexibility as compared to other techniques.

WARRANTY AND SERVICE

The Company offers a full warranty, covering parts and labor, for the first year following the purchase of its products, which warranty coverage can be extended on an annual basis by purchasing a maintenance agreement at a price of approximately 8% to 10% of the original purchase price of the product.

Generally, minor problems have been diagnosed through modem and fixed on-site by users. The Company has developed a service program using a high volume clinical site as a model. The Company plans to provide 24-hour turnaround time for any site. The Company has contracted with a third party in Europe to service the Company's customer base.

The Company trains its customers with its in-house technical staff and with a third party trainer in Europe.

PATENTS AND PROPRIETARY RIGHTS

The Company relies on a combination of patent, trade secret, copyright and trademark laws and contractual restrictions to establish and protect proprietary rights in its products and to maintain its competitive position.

The Company has filed five patent applications, and is preparing for filing additional patent applications covering various aspects of its technology. In addition, IBM has agreed not to assert infringement claims against the Company with respect to an IBM patent relating to robotic medical technology, to the extent such technology is used in the Company's products. Furthermore, significant portions of the ORTHODOC and ROBODOC System software are protected by copyrights. IBM has granted the Company a royalty-free license for the underlying software code for the ROBODOC System. In addition, the Company has registered the marks ROBODOC and ORTHODOC.

GOVERNMENT REGULATION

The medical devices to be marketed and manufactured by the Company are subject to extensive regulation by the FDA and, in some instances, by foreign and state governments. Pursuant to the Federal Food, Drug, and Cosmetic Act of 1976, as amended, and the regulations promulgated thereunder (the "FDC Act"), the FDA regulates the clinical testing, manufacturing, labeling, distribution, and promotion of medical devices. Noncompliance with applicable requirements can result in, among other things, fines, injunctions, civil penalties, recall or seizure of products, total or partial suspension of production, failure of the government to grant pre-market clearance or pre-market approval for devices, withdrawal of marketing clearances or approvals, and criminal prosecution. The FDA also has the authority to request repair, replacement or refund of the cost of any device manufactured or distributed by the Company.

Any products manufactured or distributed by the Company pursuant to the FDA clearances or approvals are subject to pervasive and continuing regulation by the FDA, including quality system requirements ("QSR"), documentation and reporting of adverse experiences with the use of the device. Device manufacturers are required to register their establishments and list their devices with the FDA and with certain state agencies and are subject to periodic compliance inspections by the FDA and certain state agencies.

As a result of a recent pre-filing meeting with representatives of the FDA, the Company intends to file a premarket approval application ("PMA") with the FDA in the second quarter of 1998 for approval to market the ROBODOC System in the United States. There can be no assurance as to when or if the FDA will grant PMA approval to the ROBODOC System or that such approval, if obtained, will not include unfavorable limitations or restrictions.

After receipt of PMA approval, if any, the Company expects that the FDA would consider new surgical applications for the ROBODOC System to be new indications for use, which generally would require FDA approval of a PMA supplement, 510(k) submission or, possibly a new PMA. The FDA is also likely to require additional approvals before the agency will permit the Company to incorporate new imaging modalities (such

as ultrasound and MRI) or other different technologies in the ROBODOC System. The FDA likely will require new clinical data to support new indications and enhanced technological characteristics.

In February 1996, the Company filed a 510(k) submission for the ORTHODOC as a stand-alone device. This 510(k) was the first product submission filed by the Company with the FDA. In January 1997, the ORTHODOC received clearance from the FDA for marketing in the United States. The NeuroMate System received 510(k) clearance from the FDA for marketing in the United States in May 1997. Medical device companies may make regulatory decisions that non-significant modifications to a 510(k) cleared product do not require additional regulatory submissions or notifications.

Labeling and promotion activities are subject to scrutiny by the FDA and, in certain instances, by the Federal Trade Commission. Current FDA enforcement policy prohibits marketing approved medical devices for unapproved uses. The Company and its products are also subject to a variety of state laws and regulations in those states or localities where its products are or will be marketed. Any applicable state or local regulations may hinder the Company's ability to market its products in those states or localities. Manufacturers are also subject to numerous federal, state and local laws relating to such matters as safe working conditions, manufacturing practices, environmental protection, fire hazard control and disposal of hazardous or potentially hazardous substances. There can be no assurance that the Company will not be required to incur significant costs to comply with such laws and regulations now or in the future or that such laws or regulations will not have a material adverse effect upon the Company's business, financial condition or results of operations.

Exports of products subject to the 510(k) notification requirements, but not yet cleared to market, are permitted without FDA export approval provided certain requirements are met. Unapproved products subject to the PMA requirements must receive prior FDA export approval unless they are approved for use by any member country of the European Union and certain other countries, including Australia, Canada, Israel, Japan, New Zealand, Switzerland and South Africa, in which case they can be exported to any country without prior FDA approval. To obtain FDA export approval, when it is required, certain requirements must be met and information must be provided to the FDA, including documentation demonstrating that the product is approved for import into the country to which it is to be exported and, in some instances, safety data from animal or human studies.

The introduction of the Company's products in foreign markets has subjected, and will continue to subject, the Company to foreign regulatory clearances which may impose additional substantive costs and burdens. International sales of medical devices are subject to the regulatory requirements of each country. The regulatory review process varies from country to country. Many countries also impose product standards, packaging requirements, labeling requirements and import restrictions on devices. In addition, each country has its own tariff regulations, duties and tax requirements.

The ROBODOC System satisfies international electromedical standard IEC 601-1 and the protection requirements of the Electromagnetic Compatibility Directive (89/336/EEC), thus allowing the Company to apply the CE Mark. This conformity is evidenced by the grant of a GS-Mark by Technische Uebermachungs Verein Rheinland ("TUV"), a testing body in Germany, under current German regulations. The ROBODOC System also satisfies the relevant provisions of the Medical Device Directive for a Class II b Medical Device.

The NeuroMate System satisfies the relevant provisions of the Medical Device Directive for a Class IIb Medical Device, thus allowing the Company to apply the CE Mark. In June 1997, the NeuroMate System received clearance from the Japanese Ministry of Health for marketing in Japan.

PRODUCT LIABILITY

The manufacture and sale of medical products exposes the Company to the risk of significant damages from product liability claims. The Company maintains product liability insurance against product liability claims in the amount of $5 million per occurrence and $5 million in the aggregate. There can be no assurance, however, that the coverage limits of the Company's insurance policies will be adequate, that the Company will continue to be able to procure and maintain such insurance coverage, or that such insurance can be maintained at acceptable costs. Although the Company has not experienced any product liability claims to

date, a successful claim brought against the Company in excess of its insurance coverage could have a materially adverse effect on the Company's business, financial condition, and results of operations.

EMPLOYEES

As of March 11, 1998, the Company had 64 full time employees, including 35 in research and development, 4 in manufacturing, 5 in regulatory affairs and quality assurance, 10 in sales and marketing and 10 in administration. Except for the employees of IMMI, none of the Company's employees is covered by a collective bargaining agreement. The Company believes its relationship with its employees is satisfactory.

ITEM 2. DESCRIPTION OF PROPERTY.

The Company's executive offices and production facilities, comprising a total of approximately 17,000 square feet of space, are located in Sacramento, California and Lyon, France. The Company occupies the facilities in Sacramento pursuant to two leases that expire on June 30, 1998. The total rent expense for these premises is approximately $12,600 per month. The lease for the Company's production facility in Sacramento provides for escalation of rent at the rate of 5% per annum. The facility in Lyon is located within a university and is provided free of charge to the Company until June 30, 1998. On September 19, 1997, the Company entered into a lease for an approximately 30,500 square foot office and production facility in Davis, California. The lease is for a term of seven years, commencing not later than September 1, 1998, and provides for rent of $27,810 per month during the first year of the lease (plus real estate taxes and assessments, utilities and maintenance), subject to adjustment in subsequent years for cumulative increases in the cost of living index, not to exceed 4% per year. The Company expects to relocate its executive offices and production facilities to the Davis, California site on or about June 1, 1998.

ITEM 3. LEGAL PROCEEDINGS.

The Company is not a party to any pending legal proceeding and its property is not subject to such proceeding.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.

No matter was submitted to a vote of security holders, through the solicitations of proxies or otherwise, during the fourth quarter of the fiscal year ended December 31, 1997.

ITEM 5. MARKET FOR COMMON EQUITY AND RELATED STOCKHOLDER MATTERS.

(a) Since November 21, 1996, the Company's Common Stock and redeemable Common Stock Purchase Warrants ("Warrants") have traded on the Nasdaq SmallCap Market under the symbols "RDOC" and "RDOCW", respectively. The Company's Common Stock and Warrants also are listed on the Pacific Exchange under the symbols "ROB" and "ROBWS", respectively.* Since November 21, 1997, the Common Stock also has been traded on EASDAQ under the symbol "RDOC."

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*No trading activity has been reported by the Pacific Exchange.

Set forth below are the high and low closing sale prices for the Common Stock and Warrants on the Nasdaq SmallCap Market for each quarter since November 21, 1996.

	COMMON STOCK ("RDOC")		WARRANTS ("RDOCW")	
QUARTER ENDED	HIGH	LOW	HIGH	LOW
December 31, 1996 (since November 21, 1996).....	$5 3/4	$5	$1	$ 1/2
March 31, 1997.....	$6 1/4	$5	$1 1/2	$ 5/8
June 30, 1997.....	$7 5/8	$5	$2 1/4	$ 7/16
September 30, 1997.....	$9 1/2	$6 1/2	$3 3/8	$1 1/2
December 31, 1997.....	$9	$3 7/8	$3 1/8	$1
March 31, 1998 (through March 23, 1998).....	$5 7/8	$3 15/16	$1 13/16	$1 1/8

(b) As of March 10, 1998, there were 74 holders of record of the Common Stock and 9 holders of record of the Warrants. The Company believes that as of March 10, 1998 there were approximately 1,090 and 470 beneficial owners of Common Stock and Warrants, respectively.

ITEM 6. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION.

The following discussion and analysis relates to the operations of Integrated Surgical Systems, Inc. and does not include the operations of IMMI, except for the results of its operations subsequent to its acquisition by the Company on September 5, 1997, and should be read in conjunction with the consolidated financial statements of Integrated Surgical Systems, Inc., including the notes thereto, appearing elsewhere in this report.

RESULTS OF OPERATIONS

Fiscal Years Ended December 31, 1997 and 1996

Net Sales. Net sales for the year ended December 31, 1997 ("Fiscal 1997") increased by approximately $2,654,000 (to approximately $4,934,000), or by 116%, as compared to Fiscal 1996 (approximately $2,280,000). This increase in net sales is largely attributable to the sale of seven and the lease of one ROBODOC Systems in Fiscal 1997, as compared to the sale of four ROBODOC Systems in Fiscal 1996. Net sales for Fiscal 1997 also include approximately $232,000 attributable to agreements between the Company and hip prostheses suppliers to incorporate software for their hip prostheses into the ROBODOC System.

Cost of Sales. Cost of sales for Fiscal 1997 was approximately $2,183,000 (44% of net sales) as compared to approximately $884,000 (39% of net sales) for Fiscal 1996. The higher cost as a percent of sales in Fiscal 1997 is a result of higher manufacturing overhead costs in Fiscal 1997 as the Company moved from its pilot manufacturing operation in Fiscal 1996 towards creating the infrastructure necessary to support on-going manufacturing and inventory adjustments resulting from components made obsolete by technical advancements to the ROBODOC System.

Selling, General and Administrative. Selling, general and administrative expenses for Fiscal 1997 (approximately $3,701,000) increased by approximately $1,635,000, or 79%, as compared to Fiscal 1996 (approximately $2,066,000). Marketing costs increased approximately $991,000 with the addition of a European sales and service staff, increased participation in medical conferences and travel to potential customer sites. General and administrative costs increased approximately $644,000 to support increased growth as well as investor relations, and the additional administrative expenses connected with the acquisition of IMMI.

Research and Development. Research and development expenses for Fiscal 1997 (approximately $3,064,000) increased by approximately $596,000, or approximately 24%, as compared to the Fiscal 1996 (approximately $2,469,000), due to additional engineering staff required to support new applications of existing products and new product development projects.

In-process Research and Development Acquired. During Fiscal 1997, the Company recorded a charge to operations in the amount of $331,668 in connection with in-process research and development acquired from IMMI on September 5, 1997. Management does not believe that the technological feasibility of the acquired in-process research and development has been established. Further, management believes the acquired in-process research and development has no alternative future uses. Therefore, the amount allocated to in-process research and development is required to be immediately expensed under generally accepted accounting principles. Although the Company is in the process of evaluating its research and development projects, it is expected that future expenditures of approximately $2,750,000 will be necessary to develop the acquired in-process technology into commercial products.

Stock Compensation. Stock compensation expense during Fiscal 1997 was approximately $155,000, approximately $202,000 lower than for Fiscal 1996 (approximately $357,000). This decrease is due to the immediate vesting of certain stock options in Fiscal 1996. The Company charged to operations in 1996 deferred stock compensation relating to stock options granted during 1996 with exercise prices less than the estimated fair value of the Company's Common Stock (as determined by an independent valuation analysis) on the date of grant. Deferred compensation for the non-vested portion is being amortized into expense over the vesting period of the stock options, which generally range from three to five years. Stock compensation expense in Fiscal 1997 represents the additional vesting which occurred in 1997.

Interest Income. Interest income for Fiscal 1997 (approximately $215,000) increased by approximately $127,000, or 144%, as compared to Fiscal 1996 (approximately $88,000), primarily due to higher average cash balances during Fiscal 1997 as a result of the Company's initial public offering in November 1996 and European offering in November 1997.

Foreign Currency Loss. Losses incurred in connection with foreign currency transactions amounted to approximately $147,000 in Fiscal 1997 as a result of exchange rates that strengthened the U.S. Dollar relative to the Deutsch Mark before the proceeds of the Company's European secondary offering could be repatriated from Deutsch Marks into U.S. Dollars. In Fiscal 1996, transaction losses were approximately $2,000.

Other Income and Expense. Other income for Fiscal 1997 amounted to approximately $32,000, as a result of the recognition of income from a grant in the Company's IMMI subsidiary, which was acquired September 5, 1997. In Fiscal 1996, other expense amounted to approximately $29,000, due primarily to losses incurred on the disposal of fixed assets.

Net Loss. The net loss for Fiscal 1997 (approximately $4,478,000) increased by approximately $1,029,000, or approximately 29.8%, as compared to the net loss for Fiscal 1996 (approximately $3,449,000), primarily due to the higher operating expenses, the write-off of IMMI in-process research and development and the amortization of identified intangible assets acquired in connection with the acquisition of IMMI.

LIQUIDITY AND CAPITAL RESOURCES

Since inception, the Company's expenses have exceeded net sales. Operations have been funded primarily from the issuance of debt and the sale of equity securities aggregating approximately $32.6 million. In addition, the Company was the beneficiary of proceeds from a $3 million key-man life insurance policy in 1993 upon the death of one of its executives.

The Company used cash from operating activities of approximately $3,432,000 and $4,421,000 in Fiscal 1996 and Fiscal 1997, respectively. Net cash used for operations in each of these periods resulted primarily from the net loss. Cash used for operations in Fiscal 1996 reflected a payment made on a note payable held by a supplier, a decrease in a customer deposit relating to the delivery of a commercial system and increases in accounts receivable and inventory. Cash used for operations in Fiscal 1997 reflected an increase in accounts receivable and inventories. The Company is eligible to receive reimbursement for 49% of its qualified expenditures under the terms of a grant from the National Institute for Standards & Technology ("NIST"). The Company received reimbursements from this program of approximately $116,000 and $317,000 for Fiscal 1996 and Fiscal 1997, respectively.

The Company's investing activities have consisted primarily of expenditures for property and equipment which totaled approximately $41,000 and $377,000 in Fiscal 1996 and Fiscal 1997, respectively, investments in sales-type leases of approximately $453,000 in Fiscal 1997 and payments in connection with the purchase of a subsidiary of $119,000 in Fiscal 1997.

Cash provided by financing activities from inception through Fiscal 1997 is comprised principally of the net cash proceeds from the sale of a convertible note in the principal amount of $3,000,000, the sale of convertible preferred stock and warrants for $14,676,000, and the sale of Common Stock and warrants for approximately $6,137,000, resulting from the Company's initial public offering in November 1996, and approximately $8,440,000 from the Company's European offering in November 1997. As part of the recapitalization of the Company in December 1995, the entire $3,000,000 principal amount of the convertible note, together with accrued interest thereon of approximately $1,224,000, was converted into a warrant to purchase Common Stock. A total of $11,734,000 and $2,942,000 of preferred stock and warrants to purchase preferred stock was converted into Common Stock and warrants to purchase common stock in December 1995 and November 1996, respectively.

The Company expects to incur additional operating losses at least through 1998. These losses will be as a result of expenditures related to product development projects and the establishment of marketing, sales, service and training organizations. The timing and amounts of these expenditures will depend on many factors, some of which are beyond the Company's control, such as the requirements for and time required to obtain FDA authorization to market the ROBODOC System, the progress of the Company's product development projects and market acceptance of the Company's products. The Company expects its current funding and cash flows from operations will be sufficient to finance its operations through 1999.

YEAR 2000 COMPLIANCE

The Company has a wide variety of computers and computer software used in the normal course of business. In predominant use throughout the Company are commercially available hardware and software products that are year 2000 compliant. Where the Company has identified any year 2000 issues, actions are underway to address them prior to the time they could impact the Company's computing requirements. It is estimated that the Company will need to spend less than $100,000 to become year 2000 compliant.

ITEM 7. FINANCIAL STATEMENTS.

The financial statements follow Item 13 of this report.

ITEM 8. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.

The Company did not have any changes in or disagreements with its accountants on accounting and financial disclosure.

ITEM III

ITEM 9. DIRECTORS, EXECUTIVE OFFICERS, AND PROMOTION AND CONTROL PERSONS; COMPLIANCE WITH SECTION 16(A) OF THE EXCHANGE ACT.

The information called for by this Item is incorporated by reference to the Company's definitive proxy statement for the 1998 Annual Meeting of Stockholders to be filed pursuant to Regulation 14A.

ITEM 10. EXECUTIVE COMPENSATION.

The information called for by this Item is incorporated by reference to the Company's definitive proxy statement for the 1998 Annual Meeting of Stockholders to be filed pursuant to Regulation 14A.

ITEM 11. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT.

The information called for by this Item is incorporated by reference to the Company's definitive proxy statement for the 1998 Annual Meeting of Stockholders to be filed pursuant to Regulation 14A.

ITEM 12. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS.

The information called for by this Item is incorporated by reference to the Company's definitive proxy statement for the 1998 Annual Meeting of Stockholders to be filed pursuant to Regulation 14A.

ITEM 13. EXHIBITS AND REPORTS ON FORM 8-K.

(a) Exhibits:

EXHIBIT	DESCRIPTION
3.1	Form of Certificate of Incorporation of the Registrant, as amended.*
3.2	By-laws of the Registrant.*
4.1	Form of warrant issued to the underwriters for the Registrant's initial public offering in November 1996.*
4.2	Form of Warrant Agreement relating to the Registrant's Redeemable Common Stock Purchase Warrants.*
4.3	Specimen Common Stock Certificate.*
4.4	Specimen Warrant Certificate (included as Exhibit A to Exhibit 4.2 herein).*
4.5	1998 Stock Option Plan.
4.6	Employee Stock Purchase Plan.
4.7	Common Stock Purchase Warrant issued by the Registrant to International Business Machines Corporation ("IBM"), dated February 6, 1991, as amended (included as Exhibit J to Exhibit 10.5 herein).*
4.8	Stockholders' Agreement between the Founders of the Registrant and IBM, dated February 6, 1991, as amended.*
4.9	Common Stock Purchase Warrant issued by the Registrant to IBM, dated December 21, 1995 (included as Exhibit I to Exhibit 10.5 herein).*
4.10	Series D Preferred Stock Purchase Warrant issued by the Company to IBM, dated December 21, 1995 (included as Exhibit H to Exhibit 10.5 herein).*
4.11	Warrant issued by the Registrant to Sutter Health, Sutter Health Venture Partners ("Sutter Health VP") and Keystone Financial Corporation ("Keystone"), dated December 21, 1995 (included as Exhibits K, L and M, respectively, to Exhibit 10.5 herein).*
4.12	Registration Rights Agreement among the Registrant, IBM, John N. Kapoor Trust ("Kapoor"), EJ Financial Investments V, L.P. ("EJ Financial"), Keystone, Sutter Health and Sutter Health VP. dated as of December 21, 1995 (included as Exhibit G to Exhibit 10.5 herein).*
4.13	1995 Stock Option Plan, as amended.*
4.14	Series D Preferred Stock Purchase Warrant issued by the Registrant to IBM, dated February 29, 1996 (together with the warrant referred to in Exhibit 4.10, the "Series D Warrants").*
4.15	Form of Lock-up Agreement.*
4.16	Letter Agreement between the Registrant and IBM dated October 29, 1997, amending the Series D Warrants and the Series D Preferred Stock and Warrant Purchase Agreement among the Registrant, IBM and EJ Financial, dated December 21, 1995.**
4.17	Form of warrant issued to CA IB Investmentbank Aktiengesellschaft and Value Management & Research GmbH**.

EXHIBIT	DESCRIPTION
10.1	Loan and Warrant Purchase Agreement between the Registrant and IBM, dated as of February 6, 1991.*
10.2	License Agreement between the Registrant and IBM, dated February 4, 1991.*
10.3	Series B Preferred Stock Purchase Agreement among the Registrant, Sutter Health and The John N. Kapoor Trust, dated as of April 10, 1992.*
10.4	Series C Preferred Stock Purchase Agreement among the Registrant, Sutter Health and Keystone, dated as of November 13, 1992, as amended December 13, 1995.*
10.5	Series D Preferred Stock and Warrant Purchase Agreement among the Registrant, IBM and EJ Financial, dated December 21, 1995.*
10.6	Investors Agreement among the Registrant, IBM, Wendy Shelton-Paul Trust, William Bargar, Brent Mittelstadt, Peter Kazanzides, Kapoor, Sutter Health, Sutter Health VP and EJ Financial, dated as of December 21, 1995 (included as Exhibit F to Exhibit 10.5 herein).*
10.7	Employment Agreement between the Registrant and Ramesh Trivedi, dated December 8, 1995.*
10.8	License Agreement between the Registrant and IBM, dated February 4, 1991.*
10.9	Agreement for the Purchase and Use of Sankyo Industrial Products between the Registrant and Sankyo Seiki (American) Inc. dated November 1, 1992. *
10.10	Stock Purchase Agreement dated as of September 5, 1997 between the Registrant and the holders of the outstanding capital stock of Innovative Medical Machines International, S.A.**
10.11	Registration Rights Agreement dated September 5, 1997 by and among the Registrant and the holders of the outstanding capital stock of Innovative Medical Machines International, S.A.**
21.1	Subsidiaries of the Registrant.**
23.1	Consent of Ernst & Young LLP, Independent Auditors
27.1	Financial Data Schedule.

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* Incorporated by reference to the Company's Registration Statement on Form SB-2 (Registration No. 3339207) declared effective on November 20, 1996.

** Incorporated by reference to the Company's Registration Statement on Form SB-2 (Registration No. 333-31481) declared effective on November 14, 1997.

(b) Reports on Form 8-K.

The Company did not file any reports on Form 8-K during the fiscal quarter ended December 31, 1997.

SIGNATURES

In accordance with Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Dated: March 25th, 1998

INTEGRATED SURGICAL SYSTEMS, INC.

By: /s/ RAMESH C. TRIVEDI	By: /s/ MARK W. WINN
Ramesh C. Trivedi, President (Principal Executive Officer)	Mark W. Winn, Chief Financial Officer (Principal Financial and Accounting Officer)

In accordance with the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant on March 25th, 1998 in the capacities indicated.

SIGNATURE	TITLE
/s/ RAMESH C. TRIVEDI Ramesh C. Trivedi	Chief Executive Officer, President and a Director (Principal Executive Officer)
/s/ MARK W. WINN Mark W. Winn	Chief Financial Officer (Principal Financial and Accounting Officer)
/s/ JAMES C. MCGRODDY James C. McGroddy	Director
/s/ JOHN N. KAPOOR John N. Kapoor	Director
/s/ PAUL A.H. PANKOW Paul A.H. Pankow	Director
Gerald D. Knudson	Director
Patrick G. Hays	Director

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

INTEGRATED SURGICAL SYSTEMS, INC.

REPORT OF ERNST & YOUNG LLP, INDEPENDENT AUDITORS

The Board of Directors and Stockholders
Integrated Surgical Systems, Inc.

We have audited the accompanying consolidated balance sheet of Integrated Surgical Systems, Inc. as of December 31, 1997, and the related consolidated statements of operations, stockholders' equity, and cash flows for the years ended December 31, 1996 and 1997. 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 generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Integrated Surgical Systems, Inc. at December 31, 1997, and the consolidated results of its operations and its cash flows for the years ended December 31, 1996 and 1997 in conformity with generally accepted accounting principles.

ERNST & YOUNG LLP

Sacramento, California
February 26, 1998

INTEGRATED SURGICAL SYSTEMS, INC.

CONSOLIDATED BALANCE SHEET
DECEMBER 31, 1997

ASSETS	
Current assets:	
Cash and cash equivalents	$ 9,091,788
Accounts receivable	1,426,542
Inventory	1,895,338
Other current assets	473,609
Total current assets	12,887,277
Net property and equipment	648,772
Leased equipment, net	177,017
Long-term net investment in sales-type leases	350,359
Intangible assets, net	3,854,018
Other assets	13,391
	$ 17,930,834
LIABILITIES AND STOCKHOLDERS' EQUITY	
Current liabilities:	
Accounts payable	$ 1,410,215
Value added taxes payable	438,682
Accrued payroll and related expenses	416,623
Customer deposits	138,672
Accrued product retrofit costs	135,348
Current portion of bank loans	268,141
Other current liabilities	469,977
Total current liabilities	3,277,658
Bank loans, long term	27,076
Note payable	143,403
Commitments and contingencies (Notes 10 and 11)	
Stockholders' equity:	
Convertible preferred stock, $0.01 par value, 5,750,000 shares authorized, no shares issued and outstanding	--
Preferred stock, $0.01 par value, 1,000,000 shares authorized; no shares issued and outstanding	--
Common stock, $0.01 par value, 15,000,000 shares authorized; 5,503,390 shares issued and outstanding	55,034
Additional paid-in capital	38,219,836
Deferred stock compensation	(239,530)
Accumulated translation adjustment	26,272
Accumulated deficit	(23,578,915)
Total stockholders' equity	14,482,697
	$ 17,930,834

See accompanying notes.

INTEGRATED SURGICAL SYSTEMS, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

	YEARS ENDED DECEMBER 31,	
	1996	1997
Net sales	$ 2,280,311	$ 4,933,824
Cost of sales	884,152	2,182,842
	1,396,159	2,750,982
Operating expenses:		
Selling, general and administrative	2,066,236	3,701,264
Research and development	2,468,535	3,063,925
Stock compensation	357,249	155,474
In-process research and development acquired	--	331,668
	4,892,020	7,252,331
Other income (expense):		
Interest income	87,933	214,913
Interest expense	--	(26,495)
Foreign currency loss	(1,619)	(147,390)
Other	(29,016)	32,028
Loss before provision for income taxes	(3,438,563)	(4,428,293)
Provision for income taxes	10,266	49,811
Net loss	$(3,448,829)	$(4,478,104)
Basic net loss per share	$ (4.78)	$ (1.20)
Weighted average common shares outstanding	721,657	3,737,318

See accompanying notes.

INTEGRATED SURGICAL SYSTEMS, INC.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

	CONVERTIBLE PREFERRED STOCK		COMMON STOCK		ADDITIONAL PAID-IN CAPITAL	DEFERRED STOCK COMPENSATION	ACCUMULATED TRANSLATION ADJUSTMENT
	SHARES	AMOUNT	SHARES	AMOUNT			
Balance at December 31, 1995	693,195	$ 6,932	273,946	$ 2,739	$17,909,532	$ --	$ 5,297
Exercise of stock options	--	--	9,592	96	587	--	--
Sale of Series D convertible preferred stock and a warrant to purchase Series D preferred stock	346,597	3,466	--	--	996,534	--	--
Sale of common stock and warrants, net of expense	--	--	1,525,000	15,250	6,122,073	--	--
Exercise of warrants	--	--	512,831	5,128	(5,128)	--	--
Conversion of Series D convertible preferred stock to common stock	(1,039,792)	(10,398)	1,039,792	10,398	--	--	--
Deferred stock compensation	--	--	--	--	783,666	(783,666)	--
Stock compensation expense	--	--	--	--	--	357,249	--
Net loss	--	--	--	--	--	--	--
Translation adjustment	--	--	--	--	--	--	3,360
Balance at December 31, 1996	--	--	3,361,161	33,611	25,807,264	(426,417)	8,657
Exercise of stock options	--	--	18,374	184	18,416	--	--
Issuance of stock options to consultant	--	--	--	--	23,270	--	--
Issuance of warrants to consultant	--	--	--	--	65,625	--	--
Acquisition of IMMI	--	--	619,355	6,194	3,883,356	--	--
Issuance of common stock to consultant	--	--	4,500	45	28,215	--	--
Sale of common stock, net of offering expenses	--	--	1,500,000	15,000	8,425,103	--	--
Stock compensation expense	--	--	--	--	(31,413)	186,887	--
Translation adjustment	--	--	--	--	--	--	17,615
Net loss	--	--	--	--	--	--	--
Balance at December 31, 1997	--	$	5,503,390	$55,034	$38,219,836	$(239,530)	$26,272

	ACCUMULATED DEFICIT	TOTAL STOCKHOLDERS' EQUITY
Balance at December 31, 1995	$(15,651,982)	$ 2,272,518
Exercise of stock options	--	683
Sale of Series D convertible preferred stock and a warrant to purchase Series D preferred stock	--	1,000,000
Sale of common stock and warrants, net of expense	--	6,137,323
Exercise of warrants	--	--
Conversion of Series D convertible preferred stock to common stock	--	--
Deferred stock compensation	--	--
Stock compensation expense	--	357,249
Net loss	(3,448,829)	(3,448,829)
Translation adjustment	--	3,360
Balance at December 31, 1996	(19,100,811)	6,322,304
Exercise of stock options	--	18,600
Issuance of stock options to consultant	--	23,270

Issuance of warrants to consultant	--	65,625
Acquisition of IMMI	--	3,889,550
Issuance of common stock to consultant	--	28,260
Sale of common stock, net of offering expenses	--	8,440,103
Stock compensation expense	--	155,474
Translation adjustment	--	17,615
Net loss	(4,478,104)	(4,478,104)
Balance at December 31, 1997	$(23,578,915)	$14,482,697

See accompanying notes.

INTEGRATED SURGICAL SYSTEMS, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS

	YEARS ENDED DECEMBER 31,	
	1996	1997
Cash flows from operating activities:		
Net loss	$(3,448,829)	$(4,478,104)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation	221,162	228,788
In-process research and development acquired	--	331,678
Amortization of intangible assets	--	279,680
Stock compensation	357,249	155,474
Issuance of stock options to consultants	--	23,270
Changes in operating assets and liabilities:		
Accounts receivable	(549,761)	(809,338)
Inventory	(283,290)	(894,739)
Other current assets	15,769	(155,998)
Accounts payable	466,796	532,121
Value added taxes payable	258,395	160,809
Accrued payroll and related expenses	156,142	126,997
Customer deposits	(344,991)	13,672
Accrued product retrofit costs	(24,652)	--
Payable to subcontractor	110,176	(139,818)
Other current liabilities	(94,852)	186,410
Note payable	(274,498)	778
Translation adjustment	3,360	17,615
Net cash used in operating activities	(3,431,824)	(4,420,705)
Cash flows from investing activities:		
Investment in sales-type lease	--	(453,250)
Principal payments received on sales-type lease	--	19,967
Purchases of property and equipment	(41,348)	(376,573)
Payments in connection with purchase of subsidiary, net of cash acquired	--	(118,880)
Decrease (increase) in other assets	(3,578)	4,446
Net cash used in investing activities	(44,926)	(924,290)
Cash flows from financing activities:		
Proceeds from bank loans	--	71,422
Payments on bank loans	--	(94,421)
Proceeds from convertible preferred stock	1,000,000	--
Net proceeds from sale of common stock and warrants	6,137,323	8,440,103
Proceeds from exercise of stock options	683	18,600
Net cash provided by financing activities	7,138,006	8,435,704
Net increase in cash and cash equivalents	3,661,256	3,090,709
Cash and cash equivalents at beginning of period	2,339,823	6,001,079
Cash and cash equivalents at end of period	$ 6,001,079	$ 9,091,788

See accompanying notes.

INTEGRATED SURGICAL SYSTEMS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. DESCRIPTION OF BUSINESS

Integrated Surgical Systems, Inc. (the "Company") was incorporated on October 1, 1990 in Delaware. The Company develops, manufactures, markets and services image-directed, robotic products for surgical applications. The Company's principal product is the ROBODOC(R) Surgical Assistant System ("ROBODOC System"), a computer-controlled surgical robot, and the Company's ORTHODOC(R) Presurgical Planner, consisting of a computer workstation that utilizes the Company's proprietary software for pre-operative surgical planning. The first application for the ROBODOC System has been directed at cementless primary total hip replacement surgery and is currently marketed to customers in Europe.

On September 5, 1997, the Company acquired all of Innovative Medical Machines International, S.A.'s ("IMMI") issued and outstanding capital stock, stock warrants and convertible debt in a transaction accounted for as a purchase (Note 3). IMMI develops, manufactures and markets image guided robotic devices for surgical applications. Its principal product is the NeuroMate(R), a computer controlled surgical robot dedicated to stereotactic neurosurgery. The accompanying statements of operations include the operating results of IMMI for the period from September 5, 1997 to December 31, 1997.

On June 1, 1994, the Company acquired all shares of Gasfabriek Thijssen Holding BV (later renamed Integrated Surgical Systems BV), a non-operating Netherlands corporation, for approximately $4,000. The acquisition was accounted for as a purchase. Integrated Surgical Systems BV purchases and licenses products and technology from Integrated Surgical Systems, Inc. for distribution in Europe and other markets.

2. SIGNIFICANT ACCOUNTING POLICIES

CONSOLIDATION

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation.

FOREIGN CURRENCY TRANSLATION

The financial position and results of operations of IMMI and Integrated Surgical Systems BV are measured using the respective local currencies. The subsidiary balance sheet accounts are translated at the year-end exchange rate and statement of operations amounts are translated at the average exchange rate for the period. Translation adjustments are recorded as a separate component of stockholders' equity. Foreign currency transaction losses were $1,619 and $147,390 during the years ended December 31, 1996 and December 31, 1997, respectively.

REVENUE RECOGNITION

Revenues from sales without significant Company obligations beyond delivery are recognized upon delivery of the products. Revenues pursuant to agreements which include significant Company obligations beyond delivery are deferred until the Company's remaining obligations are insignificant. Revenues are recognized net of any deferrals for estimated future liabilities under contractual product warranty provisions. Estimated future product retrofit costs for ROBODOC Systems sold for clinical trials have been accrued in the accompanying financial statements. Future retrofit costs are those expected to be required to update ROBODOC Systems to the equivalent level of performance expected to be approved by the Food and Drug Administration ("FDA").

RESEARCH AND DEVELOPMENT

Software development costs incurred subsequent to the determination of the product's technological feasibility and prior to the product's general release to customers are not material to the Company's financial

position or results of operations, and have been charged to research and development expense in the accompanying consolidated statements of operations. Grants received from third parties for research and development activities are recorded as reductions of expense over the term of the agreement as the related activities are conducted. Research and development costs are expensed as incurred.

CONCENTRATION OF CREDIT RISK

The Company sells its products to companies in the healthcare industry and performs periodic credit evaluations of its customers and generally does not require collateral. The Company believes that adequate provision for uncollectible accounts receivable has been made in the accompanying financial statements. The Company maintains substantially all of its cash at five financial institutions.

FINANCIAL STATEMENT ESTIMATES

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make 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 and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

CASH EQUIVALENTS

The Company invests its excess cash in high-quality debt instruments. The Company considers highly liquid investments with maturities of three months or less from the acquisition date of the instrument to be cash equivalents. The carrying amounts reported in the balance sheet for cash and cash equivalents approximate those assets' fair values. Cash equivalents consist primarily of commercial paper. At December 31, 1997, the fair value of available-for-sale securities of $7,993,467 included in cash and cash equivalents approximates their historical cost.

FAIR VALUES OF FINANCIAL INSTRUMENTS

The carrying values of the bank loans approximate their fair values as of December 31, 1997, based on current incremental borrowing rates for similar types of borrowing arrangements.

Active markets for the Company's other financial instruments that are subject to the fair value disclosure requirements of Statement of Financial Accounting Standards No. 107, which consist of long-term lease receivables and notes payable, do not exist and there are no quoted market prices for these assets and liabilities. Accordingly, it is not practicable to estimate the fair values of such financial instruments because of the limited information available to the Company and because of the significance of the cost to obtain independent appraisals for this purpose.

PROPERTY AND EQUIPMENT

Property and equipment are stated at cost. Depreciation is calculated using the straight-line method over estimated useful lives of 3 to 5 years, or the lease term, whichever is shorter.

NET INVESTMENT IN SALES-TYPE LEASES

The net investment in sales-type leases consists of the following at December 31, 1997:

Total minimum lease payments receivable	$497,855
Less unearned interest	(64,572)
Net investment in sales type leases	433,283
Less current portion	(82,924)
Long-term net investment in sales-type leases	$350,359

The following represents future minimum lease payments to be received by the Company under its net investment in sales-type leases as of December 31, 1997:

1998	$106,656
1999	106,656
2000	106,656
2001	106,656
2002	71,231
	$497,855

INVENTORY

Inventory is recorded at the lower of cost (first-in, first-out method) or market and consists of materials and supplies used in the manufacture of the ROBODOC and NeuroMate Systems. Inventory consists of the following at December 31, 1997:

Raw materials	$ 763,607
Work-in process	780,065
Finished goods	351,666
	$1,895,338

STOCK-BASED COMPENSATION

As permitted under the provisions of Statement of Financial Accounting Standards No. 123 "Accounting for Stock-Based Compensation" ("SFAS No. 123"), the Company has elected to account for stock-based compensation using the intrinsic value method prescribed by Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB No. 25"). Under the intrinsic value method, compensation cost is the excess, if any, of the quoted market price or fair value of the stock at the grant date or other measurement date over the amount an employee must pay to acquire the stock.

INCOME TAXES

The liability method is used to account for income taxes. Under this method, deferred income 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 are scheduled to be in effect when the differences are expected to reverse.

NET LOSS PER SHARE

In 1997, the Financial Accounting Standards Board ("FASB") issued Statement No. 128, Earnings per Share. Statement 128 replaced the calculation of primary and fully diluted earnings per share with basic and

diluted earnings per share. Unlike primary earnings per share, basic earnings per share excludes any dilutive effects of options, warrants and convertible securities. Diluted earnings per share is very similar to the previously reported fully diluted earnings per share. All earnings per share amounts have been presented on the basis set forth in Statement 128 (Note 9).

SIGNIFICANT CUSTOMERS AND FOREIGN SALES

The Company recognized approximately 100% of its revenues from four customers, each representing at least 10% of the Company's total revenue, during the year ended December 31, 1996 and 86% of its revenue from seven customers, each representing at least 10% of the Company's total revenue, during the year ended December 31, 1997. Foreign sales were approximately $2,280,000 and $4,919,000 for the years ended December 31, 1996 and December 31, 1997, respectively.

NEW ACCOUNTING PRONOUNCEMENTS

In June 1997, the FASB issued Statement No. 130, Reporting Comprehensive Income. Statement 130 establishes standards for reporting and disclosure of comprehensive income and its components (revenues, expenses, gains, and losses) in a full set of general-purpose financial statements. Statement 130, which is effective for fiscal years beginning after December 15, 1997, requires reclassification of financial statements for earlier periods to be provided for comparative purposes. The Company anticipates that implementing the provisions of Statement 130 will not have a significant impact on the Company's existing disclosures.

In June 1997, the FASB issued Statement No. 131, Disclosure About Segments of an Enterprise and Related Information. Statement 131 establishes standards for the way that public business enterprises report information about operating segments. It also establishes standards for related disclosures about products and services, geographic areas and major customers. Statement 131 is effective for fiscal years beginning after December 15, 1997. In the initial year of application, comparative information for earlier years must be restated. The Company anticipates that implementing the provisions of Statement 131 will not have a significant impact on the Company's existing disclosures.

RECLASSIFICATIONS

Certain amounts reported in prior years financial statements have been reclassified to conform with the 1997 presentation.

3. ACQUISITION OF IMMI

Effective September 5, 1997, ISS acquired all of IMMI's issued and outstanding capital stock, stock warrants and convertible debt in a transaction accounted for as a purchase. The purchase price included 619,355 shares of ISS common stock with a fair market value of approximately $3.9 million and liabilities assumed and acquisition costs of approximately $1.1 million. The purchase agreement places certain restrictions on the future sale of the ISS stock issued in connection with the purchase for a period of eighteen months.

The purchase price consists of the following:

619,355 shares of ISS common stock	$3,889,549
Liabilities assumed	883,044
Acquisition costs	266,085
	$5,038,678

The Company retained independent valuation professionals to assist in the values to be assigned to the individual assets acquired including the intangibles and in-process research and development. A summary of the allocation of purchase price is as follows:

Tangible assets acquired	$ 573,302
Identified intangible assets	4,133,698
In-process research and development	331,678
	$5,038,678

Intangible assets consist primarily of developed technology relating to the NeuroMate System. Accumulated amortization on intangible assets was $279,680 as of December 31, 1997. In the opinion of ISS and IMMI management, the developed technology is completed and has alternative future uses. The estimated useful lives are expected to range from 3 to 5 years. ISS management does not believe that technological feasibility of the acquired in-process research and development has been established. Further, ISS management believes the acquired in-process research and development has no alternative future uses. Therefore, the amount allocated to in-process research and development is required to be immediately expensed under generally accepted accounting principles.

The following represents unaudited proforma statement of operations information as if the acquisition of IMMI occurred on January 1, 1996.

	YEARS ENDED DECEMBER 31,	
	1996	1997
	(UNAUDITED)	
Revenue	$ 2,728,000	$ 5,554,000
Net loss	$(5,525,000)	$(5,394,000)
Basic net loss per share	$ (4.12)	$ (1.24)

The above proforma information is presented for illustrative purposes only and may not be indicative of the results that would have been obtained had the transaction actually occurred on January 1, 1996, nor is it indicative of future combined results of operations.

4. PROPERTY AND EQUIPMENT

Property and equipment consists of the following at December 31, 1997:

ROBODOC and NeuroMate System equipment	$ 664,017
Other equipment	1,111,257
Furniture and fixtures	116,128
Leasehold improvements	147,454
	2,038,856
Less accumulated depreciation	(1,390,084)
	$ 648,772

5. REVERSE STOCK SPLIT

On December 20, 1995, the Company effected a one-for-five reverse split of the Company's common stock. In November 1996, the Company effected a one-for-1.479586 reverse split of the Company's common stock. All references in the accompanying financial statements to the number of capital shares and per-share amounts have been retroactively restated to reflect the reverse splits.

6. NOTES PAYABLE AND LONG TERM DEBT

A long-term note payable was entered into between the Company and a large corporation, a representative of which was a member of the Company's Board of Directors. The corporation is also a warrant holder of the Company. Simple interest on the note payable accrued at 9.25% per annum. On December 20, 1995, the long-term note payable and accrued interest totaling $4,224,373 was converted into a warrant to purchase 126,895 shares of the Company's common stock at $0.01 per share which is currently exercisable and expires on December 31, 2005. In conjunction with the note agreement, the Company also entered into a License Agreement with this corporation whereby the corporation granted the Company the rights to the technology underlying the ROBODOC System at the time of the Company's incorporation. In consideration for this License Agreement, the Company issued to the corporation a warrant to purchase 67,587 shares of the Company's common stock at a price of $0.07 per share. This warrant expires on December 31, 2000 and has not been exercised as of December 31, 1997.

Bank loans consist of the following at December 31, 1997:

Revolving line of credit established in July 1996 for five years with an available amount of $249,150 at December 31, 1997, with interest accruing at 7.15% per annum. The amount available decreases quarterly by 5% of the original amount beginning October 1996	$ 249,150
Bank term loan with monthly principal and interest payments of approximately $1,762 over three years from May 1997, with interest accruing at 5.75% per annum	46,067
	295,217
Less current portion	(268,141)
Long-term bank loans	$ 27,076

The bank term loans are secured by substantially all of IMMI's tangible assets (with a net book value of approximately $761,000 at December 31, 1997) and guaranteed by the Company.

The Company received an interest free loan with a balance of $143,403 at December 31, 1997 from a grant organization for the development of a new system. In the case of failure of the project, the grant organization may decide to forgive all or part of the repayments. If the Company sells either a license for the related technology, the prototype developed, or articles manufactured specifically for the research project, 50% of the revenue must be paid to the grant organization in the subsequent year, up to the balance of the loan amount outstanding. According to the contract, any such payments would be considered to be an advance repayment of the loan. The Company has not made any sales of this type through December 31, 1997.

7. STOCKHOLDERS' EQUITY

COMMON STOCK

As of December 31, 1997 the Company has reserved a total of 5,762,294 shares of common stock pursuant to warrants and options outstanding and reserved for future issuance.

INITIAL PUBLIC OFFERING

In November 1996, the Company sold in its initial public offering, a total of 1,525,000 shares of common stock at $5.00 per share and 1,753,750 warrants at $0.10 per warrant. In addition, the Company sold to its underwriter warrants to purchase an additional 305,000 shares for total consideration of $10.00. The net proceeds after underwriters' commissions and fees and other costs associated with the offering were approximately $6,137,000.

Each warrant entitles the holder to purchase one share of common stock at an exercise price of $6.00 per share, subject to adjustment in certain events, at any time during the period commencing November 20, 1997, and thereafter for a period of four years. The warrants are subject to redemption by the Company at $0.10 per warrant at any time during the exercise period on not less than 30 days prior written notice to the holders of the warrants provided certain criteria regarding the price performance of the Company's common stock are met.

EUROPEAN OFFERING

On November 20, 1997, the Company sold 1,500,000 shares of Common Stock at approximately $7.00 per share in an offering to European investors (the "European Offering"). In addition, the Company sold to its underwriters in the European Offering warrants to purchase an additional 150,000 shares for nominal consideration. The net proceeds of the European Offering were approximately $8,440,000.

Each of the warrants issued to the European Offering underwriters entitles the holder to purchase one share of common stock at an exercise price of $8.26 per share at any time during the period commencing November 21, 1998, and thereafter for a period of four years.

CONVERTIBLE PREFERRED STOCK

The Company entered into a Series D preferred stock and warrant agreement during 1995. Under the terms of this agreement, the Company received $2 million in proceeds at the first closing which occurred on December 21, 1995, and granted an option to purchase additional Series D stock and a warrant to purchase Series D Stock as described below. At the first closing, the Company sold 693,195 shares of Series D preferred stock for $0.96 per share. It also sold for $1,333,333 a warrant to purchase 1,386,390 shares of Series D at $0.01 per share. The warrant expires on December 31, 2005 and has not been exercised as of December 31, 1997. The purchasers received an option to purchase an additional 346,597 shares of Series D preferred stock and a warrant to purchase an additional 693,194 shares of Series D preferred stock, all with the same terms as in the first closing. On February 19, 1996, the option holder exercised the option and the Company sold 346,597 shares of Series D preferred stock for $0.96 per share. The Company also sold a warrant for $666,667 to purchase 693,194 shares of Series D at $0.01 per share.

Series B and Series C preferred stockholders who did not purchase Series D stock were issued warrants to purchase an aggregate of 584,959 shares of the Company's common stock at a price of $0.74 per share in consideration for their consent to the terms of the recapitalization and Series D stock sale.

On August 25, 1996 and October 29, 1996, certain holders of these warrants entered into amended warrant agreements with the Company which included a provision allowing for a cashless exercise. Under the terms of the cashless exercise, these warrant holders accepted 72,126 fewer shares as consideration for not being required to make the cash exercise payment of $0.74 per share. This resulted in these warrant holders receiving 512,831 shares of Common Stock upon their exercise on August 25, 1996 and October 29, 1996.

As per the terms of the convertible preferred stock agreement, upon the closing of the Company's initial public offering in November 1996, each of the 1,039,792 shares of outstanding Series D preferred stock were automatically converted into the same number of shares of common stock.

On October 29, 1997, the Company and IBM executed an amendment to the 1995 Stock Purchase Agreement pursuant to which the Company and IBM agreed that the Series D Warrants to purchase 2,079,584 shares of Series D Preferred Stock would be exercisable only for 2,079,584 shares of Common Stock. Also on October 29, 1997, the Company delivered to CA IB Investmentbank AG ("CA IB") an agreement not to issue any shares of Common Stock, or any warrants, options or other rights to subscribe for or purchase shares of Series D Preferred Stock, or any other securities convertible into or exercisable or exchangeable for, Series D Preferred Stock, without the consent of CA IB. In addition, the Company's

management has undertaken to cause the Board of Directors to present a resolution at the next annual meeting of the Company's stockholders to amend the Company's Restated Certificate of Incorporation to eliminate the Series D Preferred Stock therefrom. There can be no assurance that such resolution will be presented by the Board of Directors, or, if presented, adopted by the Company's stockholders.

In November 1996, the Board of Directors amended, and the stockholders subsequently approved, the Company's Articles of Incorporation to authorize 1,000,000 shares of undesignated preferred stock. Preferred stock may be issued from time to time in one or more series. The Board of Directors is authorized to determine the rights, preferences, privileges and restrictions granted to and imposed upon any wholly unissued series of preferred stock and designation of any such series without any vote or action by the Company's stockholders.

ISSUANCE OF STOCK AND STOCK WARRANTS

In September 1997, the Company issued 4,500 shares of Common Stock and warrants to purchase 25,000 shares of Common Stock (with an aggregate estimated fair value of $93,885) to Rickel & Associates, Inc. for services performed in connection with the acquisition of IMMI. The warrants have an exercise price of $7.50 per share and expire in September 2002.

STOCK OPTION PLANS

The Company has elected to follow Accounting Principles Board Opinion No. 25 "Accounting for Stock Issued to Employees" and related Interpretations in accounting for its employee stock options because, as discussed below, the alternative fair value accounting provided for under FASB Statement No. 123, "Accounting for Stock-Based Compensation," requires use of option valuation models that were not developed for use in valuing employee stock options.

The Company established a stock option plan in 1991 (the "1991 Plan") and on December 13, 1995, it established a new stock option plan (the "1995 Plan"). Certain employees of the Company surrendered their options under the 1991 Plan in return for new and additional options granted under the 1995 Plan. Officers, employees, directors and consultants to the Company may participate in the Plans. Options granted under the Plans may be incentive stock options or non-statutory stock options. 1,249,070 shares of the Company's common stock have been reserved for issuance under the Plans. Options granted generally have a term of ten years from the date of the grant. The exercise price of incentive stock options granted under the Plans may not be less than 100% of the fair market value of the Company's common stock on the date of the grant. The exercise price of non-statutory stock options granted under the Plans may not be less than 85% of the fair market value of the Company's common stock on the date of the grant. For a person who, at the time of the grant, owns stock representing 10% of the voting power of all classes of Company stock, the exercise price of the incentive stock options or the non-statutory stock options granted under the Plans may not be less than 110% of the fair market value of the common stock on the date of the grant.

Pro forma information regarding net income (loss) and earnings (loss) per share is required by SFAS No. 123, which also requires that the information be determined as if the Company has accounted for its employee stock options granted subsequent to December 31, 1994 under the fair value method of that Statement. The fair value for these options was estimated at the date of grant using the Black-Scholes option pricing model with the following weighted-average assumptions for 1996 and 1997, respectively: risk-free interest rates of 5.43% and 6.00%; dividend yield of 0%; volatility factors of the expected market price of the Company's common stock of 0.50 and 0.55; and an expected life of the option of 3.2 and 4 years.

The Black-Scholes option 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, option valuation models require the input of highly subjective assumptions including the expected stock price volatility. Because the

Company's employee stock options 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 employee stock options. For purposes of pro forma disclosures, the estimated fair value of the options is amortized to expense over the vesting period. The Company's pro forma information follows:

	1996	1997
Pro forma net loss	$(3,464,434)	$(4,624,429)
Pro forma basic net loss per share	$ (4.80)	$ (1.24)

Because SFAS No. 123 is applicable only to options granted subsequent to December 31, 1994, its pro forma effect will not be fully reflected until 1999.

The following summarizes activity under the Plans for the years ended December 31, 1996 and 1997:

	NUMBER OF SHARES	WEIGHTED AVERAGE EXERCISE PRICE
Outstanding at December 31, 1995 (at $3.33 to $7.84 per share)	75,525	$4.63
Granted (at $0.07 to $5.00 per share)	951,545	0.27
Canceled (at $.07 to $7.84 per share)	(70,294)	4.08
Exercised (at $.07 to $.25 per share)	(9,592)	0.07
Outstanding at December 31, 1996 (at $0.07 to $7.84 per share)	947,184	0.42
Granted (at $5.00 to $8.88 per share)	354,334	6.60
Canceled (at $.07 to $8.25 per share)	(79,771)	4.38
Exercised (at $.07 to $3.33 per share)	(18,374)	1.01
Outstanding at December 31, 1997 (at $0.07 to $8.88 per share)	1,203,373	1.97

All options granted in 1997 were granted with option prices equal to the fair market value of the Company's stock on the grant date. The weighted average exercise price of options granted in 1997 was $6.60 and the weighted average grant date fair value of these options was $3.16.

The weighted average exercise price of options granted in 1996 with option prices less than the fair market value of the Company's stock on the grant date was $0.12 and the weighted average grant date fair value of these options was $0.89. The weighted average exercise price of options granted in 1996 with option prices equal to the fair market value of the Company's stock on the grant date was $5.00 and the weighted average grant date fair value of these options was $2.31.

The following summarizes information related to options outstanding and options exercisable at December 31, 1997:

EXERCISE PRICE	OPTIONS OUTSTANDING	WEIGHTED AVERAGE REMAINING CONTRACTUAL LIFE (IN YEARS)	OPTIONS EXERCISABLE
$0.07	852,779	8.1	580,210
$2.07	14,943	8.5	6,803
$5.00-$5.75	102,899	9.0	11,252
$6.00-$7.63	159,398	9.4	--
$8.13-$8.88	73,354	9.7	--
	1,203,373	8.5	598,265

Of the options outstanding at December 31, 1997, options to purchase 598,265 shares of common stock were immediately exercisable at a weighted-average exercise price of $0.19 per share. A total of 45,697 shares were still available for grant under the 1995 Plan at December 31, 1997.

During the year ended December 31, 1996, the Company recorded deferred stock compensation of $783,666 relating to stock options granted during the period with exercise prices less than the estimated fair value of the Company's common stock, as determined by an independent valuation analysis, on the date of grant. The deferred stock compensation is being amortized into expense over the vesting period of the stock options which generally range from 3 to 5 years. Deferred compensation relating to stock options which vested immediately was expensed on the date of grant. During 1997, the Company recorded a reduction of $31,413 in deferred stock compensation relating to canceled options. Compensation expense of $357,249 and $155,474 was recorded during the years ended December 31, 1996 and 1997, respectively, relating to these options, and the remaining $239,530 will be amortized into expense in future periods.

8. INCOME TAXES

The income tax provisions for the years ended December 31, 1996 and 1997 are comprised of currently payable state franchise taxes and currently payable foreign income taxes.

Deferred taxes result from temporary differences in the recognition of certain revenue and expense items for income tax and financial reporting purposes. The significant components of the Company's deferred taxes as of December 31, 1996 and 1997 are as follows:

	1996	1997
Deferred tax assets:		
Net operating loss carryover	$ 3,000,000	$ 4,677,000
Capitalized research and development	245,000	223,000
Accrued product retrofit costs	56,000	21,000
Inventory	85,000	93,000
Depreciation	102,000	126,000
Stock compensation	154,000	220,000
Other	158,000	158,000
	3,800,000	5,518,000
Less: Valuation allowance	(3,800,000)	(5,518,000)
Net deferred taxes	$ --	$ --

The principal reasons for the difference between the effective income tax rate and the federal statutory income tax rate are as follows:

	YEARS ENDED DECEMBER 31,	
	1996	1997
Federal benefit expected at statutory rates	$(1,172,000)	$(1,522,555)
Net operating loss with no current benefit	1,172,000	1,522,555
Other taxes	10,000	--
Foreign income taxes	266	49,811
	$ 10,266	$ 49,811

In connection with the Company's Series D preferred stock sale (Note 7) a change of ownership (as defined in Section 382 of the Internal Revenue Code of 1986, as amended) occurred. As a result of this change, the Company's federal and state net operating loss carryforwards generated through December 21,

1995 (approximately $13,500,000 and $4,500,000, respectively) will be subject to a total annual limitation in the amount of approximately $400,000. Except for the amounts described below, the Company expects that the carryforward amounts will not be available prior to the expiration of the carryforward periods.

As a consequence of the limitation, the Company has at December 31, 1997 a net operating loss carryover of approximately $11,000,000 for federal income tax purposes which expires between 2005 and 2012, a net operating loss carryforward of approximately $3,600,000 for state income tax purposes which expires through 2002, and a net operating loss carryforward of approximately $1,500,000 for foreign income tax purposes. The Company has at December 31, 1997 research and development credit carryovers of approximately $100,000 and $145,000 for federal and state income tax purposes, respectively.

The Company paid $1,600 and $914 for income and franchise taxes during the years ended December 31, 1996 and 1997, respectively.

9. NET LOSS PER SHARE INFORMATION

As of December 31, 1997, outstanding options to purchase 1,203,373 shares of common stock (with exercise prices ranging from $0.07 to $8.88) and outstanding warrants to purchase 4,507,816 shares of common stock (with exercise prices from $0.07 to $8.26) could potentially dilute basic earnings per share in the future and have not been included in the computation of diluted net loss per share because to do so would have been antidilutive for the periods presented.

10. COMMITMENTS

The Company leases its U.S. facilities under two non-cancelable operating leases. Both leases expire June 30, 1998. On September 19, 1997, the Company entered into a lease for an office and production facility in Davis, California. The lease is for a term of seven years, commencing not later than September 1, 1998, and provides for rent of $27,810 per month during the first year of the lease (plus real estate taxes and assessments, utilities and maintenance), subject to adjustment in subsequent years for cumulative increases in the cost of living index, not to exceed 4% per year.

Future payments under non-cancelable facility operating leases are approximately as follows:

1998	$ 234,000
1999	337,000
2000	344,000
2001	351,000
2002	358,000
Thereafter	925,000
	$2,549,000

Aggregate rental expense under these leases amounted to $141,456 and $135,000 during the years ended December 31, 1996 and 1997, respectively.

Future minimum payments under non-cancelable equipment operating leases are approximately as follows:

1998	$24,000
1999	24,000
2000	17,000
2001	2,000
	$67,000

Rental expense for these non-cancelable equipment operating leases during the years ended December 31, 1996 and 1997 was approximately $13,000 and $17,000, respectively.

11. CONTINGENCIES

The Company has from time to time been notified of various claims incidental to its business that are not the subject of pending litigation. While the results of claims cannot be predicted with certainty, the Company believes that the final outcome of all such matters will not have a materially adverse effect on its consolidated financial position, results of operations or cash flows.

12. NIST GRANT

During 1994, the Company received notification it was awarded a $1,960,000 National Institute of Science and Technology ("NIST") grant from the U.S. Department of Commerce ("USDC"). The grant is shared by the Company and two strategic partners to fund approximately 49% of a $4 million joint development project to adapt the ROBODOC System for use in hip revision surgery. The development project and related NIST Grant began in 1995. The Company received $116,049 and $317,000 in proceeds under this grant during the years ended December 31, 1996, and 1997, respectively.

13. ANVAR GRANT

During 1996, IMMI received notification it was awarded a $222,492 grant from the French agency Agence Nationale de Valorisation de la Recherche ("ANVAR") which is a French national agency established to aid research and development projects. The grant is to fund the clinical tests to be performed at two university hospitals on the NeuroMate system over a period of fifteen months commencing March 1997. IMMI received $173,595 in proceeds under this grant during the year ended December 31, 1997. The grant income is being recognized ratably over the project period.

EXHIBIT INDEX

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* Incorporated by reference to the Company's Registration Statement on Form SB-2 (Registration No. 3339207) declared effective on November 20, 1996.

** Incorporated by reference to the Company's Registration Statement on Form SB-2 (Registration No. 333-31481) declared effective on November 14, 1997.

EXHIBIT 4.5

INTEGRATED SURGICAL SYSTEMS, INC.
1998 STOCK OPTION PLAN

1. PURPOSE.

The INTEGRATED SURGICAL SYSTEMS, INC. 1998 STOCK OPTION PLAN (the "Plan") is intended to provide the employees, directors, independent contractors and consultants of Integrated Surgical Systems, Inc. (the "Company") and/or any subsidiary or parent thereof with an added incentive to commence and/or continue their services to the Company and to induce them to exert their maximum efforts toward the Company's success. By thus encouraging employees, directors, independent contractors and consultants and promoting their continued association with the Company, the Plan may be expected to benefit the Company and its stockholders. The Plan allows the Company to grant Incentive Stock Options ("ISOs") (as defined in Section 422(b) of the Internal Revenue Code of 1986, as amended (the "Code"), Non-Qualified Stock Options ("NQSOs") not intended to qualify under Section 422(b) of the Code and Stock Appreciation Rights ("SARs") (collectively the "Options"). The vesting of one or more Options granted hereunder may be based on the attainment of specified performance goals of the participant or the performance of the Company, one or more subsidiaries, parent and/or division of one or more of the above.

2. SHARES SUBJECT TO THE PLAN.

The total number of shares of Common Stock of the Company, $0.01 par value per share, that may be subject to Options granted under the Plan shall be 850,000 in the aggregate, subject to adjustment as provided in Paragraph 8 of the Plan; however, the grant of an ISO to an employee together with a tandem SAR or any NQSO to an employee together with a tandem SAR shall only require one share of Common Stock available subject to the Plan to satisfy such joint Option. The Company shall at all times while the Plan is in force reserve such number of shares of Common Stock as will be sufficient to satisfy the requirement of outstanding Options granted under the Plan. In the event any Option granted under the Plan shall expire or terminate for any reason without having been exercised in full or shall cease for any reason to be exercisable in whole or in part, the unpurchased shares subject thereto shall again be available for granting of Options under the Plan.

3. ELIGIBILITY.

ISO's or ISO's in tandem with SAR's (provided the SAR meets the requirements set forth in Temp. Reg. Section 14a.422A-1, A-39 (a) through (e) inclusive) may be granted from time to time under the Plan to one or more employees of the Company or of a "subsidiary" or "parent" of the Company, as the quoted terms are defined within Section 424 of the Code. An Officer is an employee for the above purposes. However, a director of the Company who is not otherwise an employee is not deemed an employee for such purposes. NQSOs and NQSO's in tandem with SARs may be granted from time to time under the Plan to one or more employees of the Company, Officers, members of the Board of Directors, independent contractors, consultants and other individuals who are not employees of, but are involved in the continuing development and success of the Company

and/or of a subsidiary of the Company, including persons who have previously been granted Options under the Plan.

4. ADMINISTRATION OF THE PLAN.

(a) The Plan shall be administered by the Board of Directors of the Company as such Board of Directors may be composed from time to time and/or by a Stock Option Committee or Compensation Committee (the "Committee") which shall be comprised of solely of at least two Outside Directors (as such term is defined in regulations promulgated from time to time with respect to Section 162(m)(4)(C)(i) of the Code) appointed by such Board of Directors of the Company. As and to the extent authorized by the Board of Directors of the Company, the Committee may exercise the power and authority vested in the Board of Directors under the Plan. Within the limits of the express provisions of the Plan, the Board of Directors or Committee shall have the authority, in its discretion, to determine the individuals to whom, and the time or times at which, Options shall be granted, the character of such Options (whether ISOs, NQSOs, and/or SARs in tandem with NQSOs, and/or SARs in tandem with ISOs) and the number of shares of Common Stock to be subject to each Option, the manner and form in which the optionee can tender payment upon the exercise of his Option, and to interpret the Plan, to prescribe, amend and rescind rules and regulations relating to the Plan, to determine the terms and provisions of Option agreements that may be entered into in connection with Options (which need not be identical), subject to the limitation that agreements granting ISOs must be consistent with the requirements for the ISOs being qualified as "incentive stock options" as provided in Section 422 of the Code, and to make all other determinations and take all other actions necessary or advisable for the administration of the Plan. In making such determinations, the Board of Directors and/or the Committee may take into account the nature of the services rendered by such individuals, their present and potential contributions to the Company's success, and such other factors as the Board of Directors and/or the Committee, in its discretion, shall deem relevant. The Board of Directors' and/or the Committee's determinations on the matters referred to in this Paragraph shall be conclusive.

(b) Notwithstanding anything contained herein to the contrary, at any time during the period the Company's Common Stock is registered pursuant to Section 12 of the Securities Exchange Act of 1934 (the "1934 Act"), the Committee, if one has been appointed to administer all or part of the Plan, shall have the exclusive right to grant Options to Covered Employees, as defined under Section 162(m)(3) of the Code (generally persons subject to Section 16 of the 1934 Act) and set forth the terms and conditions thereof. With respect to persons subject to Section 16 of the 1934 Act, transactions under the Plan are intended, to the extent possible, to comply with all applicable conditions of Rule 16b-3, as amended from time to time, (and its successor provisions) if any, under the 1934 Act and Section 162(m)(4)(C) of the Code of 1986, as amended. To the extent any provision of the Plan or action by the Board of Directors or Committee fails to so comply, it shall be deemed null and void, to the extent permitted by law and deemed advisable by the Board of Directors and/or such Committee.

5. TERMS OF OPTIONS.

Within the limits of the express provisions of the Plan, the Board of Directors or the Committee may grant either ISOs or NQSOs or SARs in tandem with NQSOs or SARs in tandem with ISOs. An ISO or an NQSO enables the optionee to purchase from the Company, at any time during a specified exercise period, a specified number of shares of Common Stock at a specified price (the "Option Price"). The optionee, if granted a SAR in tandem with a NQSO or ISO, may receive from the Company, in lieu of exercising his option to purchase shares pursuant to his NQSO or ISO, at one of the certain specified times during the exercise period of the NQSO or ISO as set by the Board of Directors or the Committee, the excess of the fair market value upon such exercise (as determined in accordance with subparagraph (b) of this Paragraph 5) of one share of Common Stock over the Option Price per share specified upon grant of the NQSO or ISO/SAR multiplied by the number of shares of Common Stock covered by the SAR so exercised. The character and terms of each Option granted under the Plan shall be determined by the Board of Directors and/or the Committee consistent with the provisions of the Plan, including the following:

(a) An Option granted under the Plan must be granted within 10 years from the date the Plan is adopted, or the date the Plan is approved by the stockholders of the Company, whichever is earlier.

(b) The Option Price of the shares of Common Stock subject to each ISO and each SAR issued in tandem with an ISO shall not be less than the fair market value of the Common Stock at the time such ISO is granted. Such fair market value shall be determined by the Board of Directors and, if the Common Stock is listed on a national securities exchange or quoted on The Nasdaq Stock Market, Inc. ("Nasdaq"), the fair market value shall be the closing price of the Common Stock on such exchange or Nasdaq, or if closing prices are not available or the Common Stock is quoted on the National Association of Securities Dealers, Inc. ("NASD") OTC Bulletin Board (the "OTC Bulletin Board") or otherwise traded in the over-the-counter market, the fair market value shall be the mean of the closing bid and asked prices of the Common Stock, as reported by Nasdaq, the NASD, the OTC Bulletin Board or the National Quotation Bureau, Inc., as the case may be, on the day on which the Option is granted or, if there is no closing price or bid or asked price on that day, the closing price or mean of the closing bid and asked prices on the most recent day preceding the day on which the Option is granted for which such prices are available. If an ISO or SAR in tandem with an ISO is granted to any individual who, immediately before the ISO is to be granted, owns (directly or through attribution) more than 10% of the total combined voting power of all classes of capital stock of the Company or a subsidiary or parent of the Company, the Option Price of the shares of Common Stock subject to such ISO shall not be less than 110% of the fair market value per share of the shares of Common Stock at the time such ISO is granted.

(c) The Option Price of the shares of Common Stock subject to an NQSO or an SAR in tandem with a NQSO granted pursuant to the Plan shall be determined by the Board of Directors or the Committee, in its sole discretion, but in no event less than 85% of the fair market value per share of the shares of Common Stock at the time of grant.

(d) In no event shall any Option granted under the Plan have an expiration date later than 10 years from the date of its grant, and all Options granted under the Plan shall be subject to earlier termination as expressly provided in Paragraph 6 hereof. If an ISO or an SAR in tandem with an ISO is granted to any individual who, immediately before the ISO is granted, owns (directly or through attribution) more that 10% of the total combined voting power of all classes of capital stock of the Company or of a subsidiary or parent of the Company, such ISO shall by its terms expire and shall not be exercisable after the expiration of five (5) years from the date of its grant.

(e) An SAR may be exercised at any time during the exercise period of the ISO or NQSO with which it is granted in tandem and prior to the exercise of such ISO or NQSO. Notwithstanding the foregoing, the Board of Directors and/or the Committee shall in their discretion determine from time to time the terms and conditions of SAR's to be granted, which terms may vary from the afore-described conditions, and which terms shall be set forth in a written stock option agreement evidencing the SAR granted in tandem with the ISO or NQSO. The exercise of an SAR granted in tandem with an ISO or NQSO shall be deemed to cancel such number of shares subject to the unexercised Option as were subject to the exercised SAR. The Board of Directors or the Committee has the discretion to alter the terms of the SARS if necessary to comply with Federal or state securities law. Amounts to be paid by the Company in connection with an SAR may, in the Board of Director's or the Committee's discretion, be made in cash, Common Stock or a combination thereof.

(f) An Option granted under the Plan shall become exercisable, in whole at any time or in part from time to time, but in no event may an Option (i) be exercised as to less than one hundred (100) shares of Common Stock at any one time, or the remaining shares of Common Stock covered by the Option if less than one hundred (100), and (ii) except with respect to performance based Options, become fully exercisable more than five years from the date of its grant nor shall less than 20% of the Option become exercisable by the end of any of the first five years of the Option, determined on an aggregate basis, if not terminated as provided in Paragraph 6 hereof. The Board of Directors or the Committee, if applicable, shall, in the event it so elects in its sole discretion, set one or more performance standards with respect to one or more Options upon which vesting is conditioned (which performance standards may vary among the Options).

(g) An Option granted under the Plan shall be exercised by the delivery by the holder thereof to the Company at its principal office (to the attention of the Secretary) of written notice of the number of full shares of Common Stock with respect to which the Option is being exercised, accompanied by payment in full, which payment at the option of the optionee shall be in the form of (i) cash or certified or bank check payable to the order of the Company, of the Option Price of such shares of Common Stock, or, (ii) if permitted by the Committee or the Board of Directors, as determined by the Committee or the Board of Directors in its sole discretion at the time of the grant of the Option with respect to an ISO and at or prior to the time of exercise with respect to a NQSO, by the delivery of shares of Common Stock having a fair market value equal to the Option Price or the delivery of an interest-bearing promissory note having an original principal balance equal to the Option Price and an interest rate not below the rate which would result in imputed interest under the Code (provided, in order to qualify as an ISO, more than one year shall have passed since the date

of grant and one year from the date of exercise), or (iii) at the option of the Committee or the Board of Directors, determined by the Committee or the Board of Directors in its sole discretion at the time of the grant of the Option with respect to an ISO and at or prior to the time of exercise with respect to a NQSO, by a combination of cash, promissory note and/or such shares of Common Stock (subject to the restriction above) held by the employee that have a fair market value together with such cash and principal amount of any promissory note that shall equal the Option Price, and, in the case of any Option at the discretion of the Committee or Board of Directors by having the Company withhold from the shares of Common Stock to be issued upon exercise of the Option that number of shares having a fair market value equal to the exercise price and/or the tax withholding amount due, or otherwise provide for withholding as set forth in Paragraph 9(c) hereof, or in the event an employee is granted an ISO or NQSO in tandem with an SAR and desires to exercise such SAR, such written notice shall so state such intention. To the extent allowed by applicable Federal and state securities laws, the Option Price may also be paid in full by a broker-dealer to whom the optionee has submitted an exercise notice consisting of a fully endorsed Option, or through any other medium of payment as the Board of Directors and/or the Committee, in its discretion, shall authorize.

(h) The holder of an Option shall have none of the rights of a stockholder with respect to the shares of Common Stock covered by such holder's Option until such shares of Common Stock shall be issued to such holder upon the exercise of the Option.

(i) All Options granted under the Plan shall not be transferable, except by will or the laws of descent and distribution and may be exercised during the lifetime of the holder thereof only by the holder. No Option granted under the Plan shall be subject to execution, attachment or other process.

(j) The aggregate fair market value, determined as of the time any ISO or SAR in tandem with an ISO is granted and in the manner provided for by Subparagraph (b) of this Paragraph 5, of the shares of Common Stock with respect to which ISOs granted under the Plan are exercisable for the first time during any calendar year and under incentive stock options qualifying as such in accordance with Section 422 of the Code granted under any other incentive stock option plan maintained by the Company or its parent or subsidiary corporations, shall not exceed $100,000. Any grant of Options in excess of such amount shall be deemed a grant of a NQSO.

(k) Notwithstanding anything contained herein to the contrary, an SAR which was granted in tandem with an ISO shall (i) expire no later than the expiration of the underlying ISO; (ii) be for no more than 100% of the spread at the time the SAR is exercised; (iii) only be exercised when the underlying ISO is eligible to be exercised; and (iv) only be exercisable when there is a positive spread.

(l) In no event shall an employee be granted Options for more than 150,000 shares of Common Stock during any calendar year period; provided, however, that the limitation set forth in this Section 5(1) shall be subject to adjustment as provided in Section 8 herein.

6. DEATH OR TERMINATION OF EMPLOYMENT/CONSULTING RELATIONSHIP.

(a) Except as provided herein, or otherwise determined by the Board of Directors or the Committee in its sole discretion, upon termination of employment with the Company voluntarily by the employee or termination of a consulting relationship with the Company prior to the termination of the term thereof, a holder of an Option under the Plan may exercise such Options to the extent such Options were exercisable as of the date of termination at any time within thirty (30) days after termination, subject to the provisions of Subparagraph (d) of this Paragraph 6. Except as provided herein, or otherwise determined by the Board of Directors or the Committee in its sole discretion, if such employment or consulting relationship shall terminate for any reason other than death, voluntary termination by the employee or for cause, then such Options may be exercised at anytime within three (3) months after such termination. Notwithstanding anything contained herein to the contrary, unless otherwise determined by the Board of Directors or the Committee in its sole discretion, any options granted hereunder to an Optionee and then outstanding shall immediately terminate in the event the Optionee is terminated for cause, and the other provisions of this Paragraph 6 shall not be applicable thereto. For purposes of this Paragraph 6, termination for cause shall be deemed the decision of the Company, in its sole discretion, that Optionee has not adequately performed the services for which he/she/it was hired.

(b) If the holder of an Option granted under the Plan dies (i) while employed by the Company or a subsidiary or parent corporation or while providing consulting services to the Company or a subsidiary or parent corporation or (ii) within three (3) months after the termination of such holder's employment/consulting, such Options may, subject to the provisions of subparagraph (d) of this Paragraph 6, be exercised by a legatee or legatees of such Option under such individual's last will or by such individual's personal representatives or distributees at any time within such time as determined by the Board of Directors or the Committee in its sole discretion, but in no event less than six months after the individual's death, to the extent such Options were exercisable as of the date of death or date of termination of employment, whichever date is earlier.

(c) If the holder of an Option under the Plan becomes disabled within the definition of Section 22(e)(3) of the Code while employed by the Company or a subsidiary or parent corporation, such Option may, subject to the provisions of subparagraph (d) of this Paragraph 6, be exercised at any time within six months after such holder's termination of employment due to the disability.

(d) Except as otherwise determined by the Board of Directors or the Committee in its sole discretion, an Option may not be exercised pursuant to this Paragraph 6 except to the extent that the holder was entitled to exercise the Option at the time of termination of employment, consulting relationship or death, and in any event may not be exercised after the original expiration date of the Option. Notwithstanding anything contained herein which may be to the contrary, such termination or death prior to vesting shall, unless otherwise determined by the Board of Directors or Committee, in its sole discretion, be deemed to occur at a time the holder was not entitled to exercise the Option.

(e) The Board of Directors or the Committee, in its sole discretion, may at such time or times as it deems appropriate, if ever, accelerate all or part of the vesting provisions with respect to one or more outstanding options. The acceleration of one Option shall not infer that any other Option is or to be accelerated.

7. LEAVE OF ABSENCE.

For the purposes of the Plan, an individual who is on military or sick leave or other bona fide leave of absence (such as temporary employment by the Government) shall be considered as remaining in the employ of the Company or of a subsidiary or parent corporation for ninety (90) days or such longer period as such individual's right to reemployment is guaranteed either by statute or by contract.

8. ADJUSTMENT UPON CHANGES IN CAPITALIZATION.

(a) In the event that the outstanding shares of Common Stock are hereafter changed by reason of recapitalization, reclassification, stock split-up, combination or exchange of shares of Common Stock or the like, or by the issuance of dividends payable in shares of Common Stock, an appropriate adjustment shall be made by the Board of Directors, as determined by the Board of Directors and/or the Committee, in the aggregate number of shares of Common Stock available under the Plan, in the number of shares of Common Stock issuable upon exercise of outstanding Options, and the Option Price per share. Subject to subparagraph (b) of this Paragraph 8, in the event of any consolidation or merger of the Company with or into another company, or the conveyance of all or substantially all of the assets of the Company to another company for solely stock and/or securities, each then outstanding Option shall upon exercise thereafter entitle the holder thereof to such number of shares of Common Stock or other securities or property to which a holder of shares of Common Stock of the Company would have been entitled to upon such consolidation, merger or conveyance; and in any such case appropriate adjustment, as determined by the Board of Directors of the Company (or successor entity) shall be made as set forth above with respect to any future changes in the capitalization of the Company or its successor entity. In the event of the proposed dissolution or liquidation of the Company, subject to subparagraph (b) of this Paragraph 8, the sale of substantially all the assets of the Company for other than stock and/or securities, all outstanding Options under the Plan will automatically terminate, unless otherwise provided by the Board of Directors of the Company or any authorized committee thereof.

(b) Any Option granted under the Plan, may, at the discretion of the Board of Directors of the Company and said other corporation, be exchanged for options to purchase shares of capital stock of another corporation which the Company, and/or a subsidiary thereof is merged into, consolidated with, or all or a substantial portion of the property or stock of which is acquired by said other corporation or separated or reorganized into. The terms, provisions and benefits to the optionee of such substitute option(s) shall in all respects be identical to the terms, provisions and benefits of optionee under his Option(s) prior to said substitution. To the extent the above may be inconsistent with Sections 424(a)(1) and (2) of the Code, the above shall be deemed interpreted so as to comply therewith.

(c) Any adjustment in the number of shares of Common Stock shall apply proportionately to only the unexercised portion of the Options granted hereunder. If fractions of shares of Common Stock would result from any such adjustment, the adjustment shall be revised to the next higher whole number of shares of Common Stock.

9. FURTHER CONDITIONS OF EXERCISE.

(a) Unless the shares of Common Stock issuable upon the exercise of an Option have been registered with the Securities and Exchange Commission pursuant to the Securities Act of 1933, as amended, prior to the exercise of the Option, an optionee must represent in writing to the Company that such shares of Common Stock are being acquired for investment purposes only and not with a view towards the further resale or distribution thereof, and must supply to the Company such other documentation as may be required by the Company, unless in the opinion of counsel to the Company such representation, agreement or documentation is not necessary to comply with said Act.

(b) The Company shall not be obligated to deliver any shares of Common Stock until they have been listed on each securities exchange (including for this purpose, the Nasdaq Stock Market, Inc.) on which the shares of Common Stock may then be listed or until there has been qualification under or compliance with such state or federal laws, rules or regulations as the Company may deem applicable.

(c) The Board of Directors or Committee may make such provisions and take such steps as it may deem necessary or appropriate for the withholding of any taxes that the Company is required by any law or regulation of any governmental authority, whether federal, state or local, domestic or foreign, to withhold in connection with the exercise of any Option, including, but not limited to, (i) the withholding of payment of all or any portion of such Option and/or SAR until the holder reimburses the Company for the amount the Company is required to withhold with respect to such taxes, or (ii) the canceling of any number of shares of Common Stock issuable upon exercise of such Option and/or SAR in an amount sufficient to reimburse the Company for the amount it is required to so withhold, (iii) the selling of any property contingently credited by the Company for the purpose of exercising such Option, in order to withhold or reimburse the Company for the amount it is required to so withhold, or (iv) withholding the amount due from such employee's wages if the employee is employed by the Company or any subsidiary thereof.

10. TERMINATION, MODIFICATION AND AMENDMENT.

(a) The Plan (but not Options previously granted under the Plan) shall terminate ten (10) years from the earliest of the date of its adoption by the Board of Directors, or the date the Plan is approved by the stockholders of the Company, or such date of termination, as hereinafter provided, and no Option shall be granted after termination of the Plan.

(b) The Plan may from time to time be terminated, modified or amended by the affirmative vote of the holders of a majority of the outstanding shares of capital stock of the Company entitled to vote thereon.

(c) The Board of Directors of the Company may at any time, prior to ten (10) years from the earlier of the date of the adoption of the Plan by such Board of Directors or the date the Plan is approved by the stockholders, terminate the Plan or from time to time make such modifications or amendments of the Plan as it may deem advisable; provided, however, that the Board of Directors

shall not, without approval by the affirmative vote of the holders of a majority of the outstanding shares of capital stock of the Company present in person or by proxy at an Annual or Special Meeting of the Stockholders and voting thereon, increase (except as provided by Paragraph 8) the maximum number of shares of Common Stock as to which Options or shares may be granted under the Plan, or materially change the standards of eligibility under the Plan.

(d) No termination, modification or amendment of the Plan may adversely affect the rights under any outstanding Option without the consent of the individual to whom such Option shall have been previously granted.

11. EFFECTIVE DATE OF THE PLAN.

The Plan shall become effective upon adoption by the Board of Directors of the Company. The Plan shall be subject to approval by the affirmative vote of the holders of a majority of the outstanding shares of capital stock of the Company present in person or by proxy at an Annual or Special Meeting of the Stockholders and voting thereon within one year after adoption of the Plan by the Board of Directors.

12. NOT A CONTRACT OF EMPLOYMENT OR FOR SERVICES.

Nothing contained in the Plan or in any option agreement executed pursuant hereto shall be deemed to confer upon any individual to whom an Option is or may be granted hereunder any right to remain in the employ of or be engaged by the Company or of a subsidiary or parent of the Company or in any way limit the right of the Company, or of any parent or subsidiary thereof, to terminate the employment of any employee or engagement of any consultant.

13. OTHER COMPENSATION PLANS.

The adoption of the Plan shall not affect any other stock option plan, incentive plan or any other compensation plan in effect for the Company, nor shall the Plan preclude the Company from establishing any other form of stock option plan, incentive plan or any other compensation plan.

14. DISTRIBUTION OF FINANCIAL STATEMENTS.

The Company shall provide copies of the Company's annual financial statements for its most recently completed fiscal year to each person granted or exercising an option pursuant to the Plan as long as that person continues to hold such options or shares. The Company shall not be required to provide such financial statements to key employees whose duties in connection with the Company assure their access to equivalent information.

EXHIBIT 4.6

INTEGRATED SURGICAL SYSTEMS, INC.
EMPLOYEE STOCK PURCHASE PLAN

1. PURPOSE.

The purpose of the INTEGRATED SURGICAL SYSTEMS, INC. EMPLOYEE STOCK PURCHASE PLAN (the "Plan") is to provide eligible employees of Integrated Surgical Systems, Inc. (the "Company") and its subsidiaries who wish to become stockholders of the Company, an opportunity to acquire a proprietary interest in the Company through the purchase of Common Stock of the Company on a payroll deduction or other compensation deduction basis. It is believed that participation in the ownership of the Company will be to the mutual benefit of the eligible employees and the Company.

2. DEFINITIONS.

(a) "Base Pay" means regular straight time earnings, excluding payments for overtime, bonuses, incentive compensation and other special payments.

(b) "Common Stock" means the Company's $.01 par value Common Stock.

(c) "Employee" means any person, including any officer who is customarily employed by the Company or any subsidiary of the Company for more than thirty (30) hours per week and more than five (5) months in a calendar year. It is the intent of the Plan to cover all employees in full time, permanent positions.

(d) "Excess Employee Pay" means payments of compensation to Employees other than Base Pay and overtime.

(e) "Participants" means eligible Employees electing to participate in the Plan.

(f) "Subsidiary" of the Company means any company, as currently defined in Section 425(f) of the Internal Revenue Code of 1986, as amended, 50% or more of the voting shares of which are owned directly or indirectly by the Company (the term "Company" shall hereinafter be deemed to include all Subsidiaries of the Company).

3. ELIGIBILITY.

All Employees of the Company who have been employed by the Corporation for 6 months or more shall be eligible Employees.

4. ADMINISTRATION.

The Plan shall be administered by a committee designated by the Board of Directors, consisting of not less than three members (the "Committee"). Each member of the

Committee shall be either a director, an officer or an employee of the Company. The Committee shall be vested with full authority to make, administer and interpret such rules and regulations as it deems necessary to administer the Plan, and any determination, decision or action of the Committee in connection with the construction, interpretation, administration and application of the Plan shall be final, conclusive and binding upon all Participants and any and all persons claiming under or through any Participant.

5. STOCK.

(a) The Common Stock to be sold to Participants under the Plan may, at the election of the Company, be either treasury shares, shares acquired on the open market, and/or shares originally issued for such purpose. The maximum number of shares of Common Stock which shall be made available for sale under the Plan shall be 300,000 shares, as and subject to adjustment upon changes in the capitalization of the Company as provided in subparagraph (b) below. If the total number of shares which would otherwise have been acquired under the Plan on any date exceeds the number of shares of Common Stock then available under the Plan (after deduction of all shares of Common Stock for which options have been exercised or are then outstanding), the Company shall make a pro rata allocation of the shares remaining available in as nearly a uniform manner as shall be practicable and as it shall determine to be equitable. In such event, the payroll deductions to be made pursuant to the authorizations therefor shall be reduced accordingly and the Company shall give written notice of such reduction to each employee affected thereby.

(b) Appropriate adjustments in the maximum number of shares of Common Stock which shall be made available for sale under the Plan shall be made to give effect to any mergers, consolidations, acquisitions, stock splits, stock dividends, or other relevant changes in the capitalization of the Company occurring after the effective date of the Plan, provided that no fractional shares shall be subject to an option and each option shall be adjusted downward to the nearest full share. The establishment of the Plan or the granting of any options thereunder shall not affect in any way the right or power of the Company to make adjustments, reclassifications, reorganizations or changes in its capital or business structure or to merge, consolidate, dissolve, liquidate, sell or otherwise transfer all or any part of its business or assets.

(c) A Participant will not have any interest in shares covered by his or her authorized payroll deduction or authorized deduction from other compensation until shares of Common Stock are acquired for his or her account.

6. PARTICIPATION.

(a) After the effective date, as determined under Paragraph 16 hereof, an eligible Employee may become a Participant in the Plan by completing an authorization form for a payroll deduction or a deduction from other compensation on the form provided by the Committee. Such authorization shall become effective on the first day of the next succeeding month following the delivery of the authorization form to the Committee; provided, however, if the authorization form is delivered to the Committee less than fifteen (15) days prior to the end of any month, it shall become

effective on the first day of the second succeeding month following delivery of the authorization form to the Committee.

(b) At the time a Participant who is an Employee files his or her authorization for a payroll deduction, he or she shall elect to have weekly deductions made from his or her pay, such deductions to continue on a weekly basis until the Employee withdraws from the Plan or otherwise becomes ineligible to participate in the Plan. Authorized payroll deductions shall be a minimum of $5 per week, up to a maximum of fifteen (15%) percent of the Employee's weekly Base Pay.

(c) Within ten (10) days after a Participant who is an Employee receives notice, either individually or as part of a group, or otherwise becomes aware that the Participant will receive Excess Employee Pay, the participant may elect to have a deduction therefrom in an amount not to exceed fifteen (15%) percent of the Excess Employee Pay to be paid at such time. If a payment of Excess Employee Pay is payable prior to ten (10) days from notice thereof, the Employee shall have such lesser time, but in no event less than one day, to decide to have a deduction therefrom.

(d) A Participant may alter the rate of his or her deduction with respect to Base Pay within the foregoing prescribed limits by filing a new authorization form with the Committee; provided, however, alterations in the rate of deductions may not be made more frequently than once every three (3) months. An authorization to alter the rate of a Participant's deduction shall become effective on the first day of the next succeeding month following the delivery form; provided, however, if the authorization form is delivered less than fifteen (15) days prior to the end of any month, it shall become effective on the first day of the second succeeding month following delivery of the authorization form to the Committee.

(e) All compensation deductions made for a Participant shall be credited to the Participant's account under the Plan. A Participant may not make any separate cash payment into such account.

(f) All Employees granted options hereunder shall have the same rights and privileges, except that the amount of Common Stock which may be purchased by an Employee under such option shall bear a uniform relationship to the Base Pay of all Employees.

7. GRANTING OF OPTION.

(a) On the date when a Participant's authorization form for a deduction becomes effective, the Participant shall be granted a monthly option for as many full shares of Common Stock as he or she will be able to purchase with the compensation deductions credited to the Participant's account during his or her participation in the Plan during such month. The option shall continue to be effective on the first date of each successive month that the Plan is in existence and the Employee is a participant.

(b) The option price of shares of Common Stock purchased with deductions for a Participant therein shall be eighty-five percent (85%) of the closing price of the Common Stock on

The Nasdaq Stock Market, Inc. or national stock exchange on which the Common Stock is then included for quotation or listed at the time the Common Stock is acquired by the Committee on behalf of the Participant.

8. PURCHASE OF SHARES.

No less frequently than monthly, the Committee shall determine the aggregate compensation deductions for the preceding month for each Participant to purchase from the Company the shares of Common Stock which the accumulated payroll deductions on his or her account at such time may purchase at the applicable option price. Administrative and commission costs on purchases made from compensation deductions shall be paid by the Company. The Committee will cause to be delivered to each Participant a quarterly statement showing the number of shares in his or her account, the number of shares purchased for him or her in the preceding month, his or her aggregate compensation deductions for the preceding month, the average price per share paid for the shares purchased for him or her during the preceding month, and the amount of cash remaining in his or her account at the end of the month. Any dividends paid on Common Stock held in the Participant's account will be added to his or her account and any cash dividends will be added to any additional payroll deductions to purchase Common Stock as provided herein. A Participant may request delivery to him or her of the Common Stock held in the Participant's account at any time and the delivery thereof shall be made at such regular time as the Company's transfer agent shall determine. If such delivery is required at a time other than the normal monthly transfer date set by the transfer agent, the Participant requesting such transfer shall pay the costs thereof. If a Participant wishes to sell shares in his or her account, the Participant may notify the Committee to sell same, in which event all commission costs incurred in connection with the sale of the shares shall be borne by the Participant. The Company shall pay administrative costs associated therewith other than costs arising from a sale occurring at a time different from the prearranged dates set by the transfer agent for making such sales under its agreement with the Company.

9. WITHDRAWAL.

A Participant may withdraw from the Plan at any time by notifying the Committee in writing of the Participant's intent to withdraw. If such notice of withdrawal is received by the Committee prior to the 15th day of any month, such withdrawal shall become effective immediately and all compensation deductions made on behalf of the Participant during the month in which the withdrawal is made shall be paid to the Participant within 15 days after the notice of withdrawal is received by the Committee. If the notice of withdrawal is received by the Committee after the 15th day of any month, such withdrawal shall become effective on the first day of the following month and the Company shall continue to make compensation deductions on behalf of the Participant for the remainder of the month in which such notice of withdrawal is delivered to the Committee. If any Participant withdraws from the Plan, no further compensation deductions will be made on his or her behalf after the effective date of his or her withdrawal except in accordance with a new authorization form filed with the Committee as provided in Paragraph 6 hereof. Upon withdrawal from the Plan, a Participant will not be permitted to reenter the Plan until six (6) months have elapsed from the date

his or her withdrawal becomes effective. Any restrictions on the transferability of shares set forth in Paragraph 8 hereof shall survive withdrawal from the Plan and termination of services.

10. INELIGIBILITY.

If an Employee becomes ineligible to participate in the Plan at any time, all compensation deductions made on behalf of the Employee which have not been used to purchase shares of Common Stock shall be paid to the Employee within fifteen (15) days after the Committee determines that the Employee is not eligible to participate in the Plan.

11. DESIGNATION OF BENEFICIARY.

A Participant may file a written designation of a beneficiary who is to receive any shares of Common Stock credited to the Participant's account under the Plan in the event of such Participant's death prior to delivery to the Participant of the certificates for such shares. Such designation of beneficiary may be changed by the Participant at any time by written notice given in accordance with rules and procedures established by the Committee. Upon the death of a Participant and upon receipt by the Company of proof of the identity and existence, at the Participant's death, of a beneficiary validly designated by the Participant under the Plan, the Company shall deliver such shares to such beneficiary. In the event of the death of the Participant and in the absence of a beneficiary validly designated under the Plan who is living at the time of such Participant's death, the Company shall deliver such shares to the executor or administrator of the estate of the Participant, or if no such executor or administrator has been appointed, the Company, in its discretion, may deliver such shares to the spouse or to any one or more dependents or relatives of the Participant, or to such other person as the Company may designate on behalf of the estate of such deceased Participant.

12. TRANSFERABILITY.

Neither compensation deductions credited to a Participant's account nor any rights with regard to (i) the participation in the Plan or (ii) exercise of any option or (iii) the right to receive shares of Common Stock under the Plan may be assigned, transferred, pledged, or otherwise disposed of in any way by a Participant other than by will or the laws of descent and distribution; provided, however, that shares of Common Stock purchased on behalf of the Participant and left in his or her account will be subject to his or her absolute control. Any such attempted assignment, transfer, pledge, or other disposition shall be without effect, except that the Company may treat such act as an election by such Participant to withdraw from the Plan in accordance with Paragraph 9 hereof.

13. ACCOUNTS.

No compensation deductions received or held by the Company under the Plan pending the purchase of the shares may be used by the Company for any corporate purpose. The Company shall segregate such compensation deductions in separate accounts in a reasonably prudent time after the deduction is made.

14. AMENDMENT OR TERMINATION.

The Board of Directors of the Company may at any time terminate the Plan or amend the Plan in any respect. No such termination shall affect options previously granted, nor may an amendment make any change in any option theretofore granted which would adversely affect the rights of any Participant nor may an amendment be made without prior approval of the shareholders of the Company if such amendment would:

(a) Require the sale of more shares of Common Stock than are authorized under Paragraph 5 hereof; or

(b) Permit compensation deductions at a rate in excess of the rate set forth herein.

15. NOTICES.

All notices or other communications by a Participant under or in connection with the Plan shall be deemed to have been duly given when received in writing by the Chief Financial Officer of the Company or when received in the form specified by the Committee at the location and by the person designated by the Committee for the receipt thereof.

16. EFFECTIVE DATE AND APPROVALS

The Plan shall become effective at a time when:

(a) the Plan has been adopted by the Board of Directors of the Company; and

(b) a registration statement on Form S-8 under the Securities Act of 1933, as amended, has become effective with respect to the Plan; and

(c) the Company has received an opinion of counsel that there has been compliance with all federal and state securities laws including, without limitation, applicable state blue sky laws; and

(d) the Committee has notified the eligible Employees of the Company that they may commence participation in the Plan; and

(e) the Plan is approved by the affirmative vote of holders of a majority of the shares of capital stock of the Company present at an Annual or Special Meeting of Stockholders and entitled to vote thereon which approval must occur within the period ending twelve (12) months after the date the Plan is adopted by the Board of Directors.

EXHIBIT 23.1

CONSENT OF ERNST & YOUNG LLP, INDEPENDENT AUDITORS

We consent to the incorporation by reference in the Registration Statement (Form S-3 No. 333-42051) of Integrated Surgical Systems, Inc. and in the related Prospectus of our report dated February 26, 1998, with respect to the consolidated financial statements of Integrated Surgical Systems, Inc. included in this Annual Report (Form 10-KSB) for the year ended December 31, 1997.

We also consent to the incorporation by reference in the Registration Statement (Form S-8 No. 333-44093) pertaining to the 1995 Stock Option Plan of Integrated Surgical Systems, Inc. of our report dated February 26, 1998, with respect to the consolidated financial statements of Integrated Surgical Systems, Inc. included in this Annual Report (Form 10-KSB) for the year ended December 31, 1997.

ERNST & YOUNG LLP

Sacramento, California
March 23, 1998

YEAR	YEAR
DEC-31-1996	DEC-31-1997
DEC-31-1996	DEC-31-1997
6,001,079	9,091,788
0	0
600,568	1,426,542
0	0
1,030,262	1,895,338
7,760,557	12,887,277
1,256,241	2,038,856
1,005,204	1,390,084
8,029,431	17,930,834
1,707,127	3,277,658
0	0
0	0
0	0
33,611	55,034
6,288,690	14,427,663
8,029,431	17,930,834
2,280,311	4,933,824
2,280,311	4,933,824
884,152	2,182,842
4,892,020	7,252,331
(57,298)	73,056
0	0
0	0
(3,438,563)	(4,428,293)
10,266	49,811
(3,448,829)	(4,478,104)
0	0
0	0
0	0
(3,448,829)	(4,478,104)
(4.78)	(1.20)
(4.78)	(1.20)