NUTRASTAR INC
Form 10QSB/A
June 05, 2002

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-QSB/A

(Amendment No. 1)

[X] QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2002

[ ] TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE EXCHANGE ACT FOR THE TRANSITION PERIOD FROM _______________ to _______________

Commission File Number 0-32565

NUTRASTAR INCORPORATED
(Exact name of small business issuer as specified in its charter)

CALIFORNIA	87-0673375
(State of other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
1261 Hawk's Flight Court El Dorado Hills, California	95762
(Address of Principal Executive Offices)	(Zip Code)

Issuer's telephone number: (916) 933-7000

Indicate by check mark whether the issuer (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the issuer was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days:

YES X NO ____

Common stock, no par value, 21,802,853 issued and outstanding as of April 30, 2002.

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PART 1 - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

PART 1 - FINANCIAL INFORMATION

NUTRASTAR INCORPORATED AND SUBSIDIARIES
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CONDENSED, CONSOLIDATED FINANCIAL STATEMENTS

NUTRASTAR INCORPORATED AND SUBSIDIARIES
CONDENSED, CONSOLIDATED BALANCE SHEET
March 31, 2002 (unaudited)

ASSETS
(restated)

Current assets	
Cash	$ 43,620
Accounts receivable	34,485
Inventory	193,966
Prepaid expenses	22,661
Total current assets	294,732
Property and equipment, net	225,133
Patents and trademarks, net	114,027
Goodwill	250,001
Deposits	136,495
Total assets	$1,020,388

The accompanying notes are an integral part of these financial statements.

NUTRASTAR INCORPORATED AND SUBSIDIARIES
CONDENSED, CONSOLIDATED BALANCE SHEET
March 31, 2002 (unaudited)

LIABILITIES AND SHAREHOLDERS' DEFICIT
(restated)

Current liabilities	
Accounts payable	$ 524,398
Accrued salaries and benefits	88,577
Accrued expenses	85,654
Due to officer	12,759
Note payable to officer	100,000
Total current liabilities	811,388
Put option	130,000
Total liabilities	941,388
Contingencies	
Convertible, redeemable series A preferred stock, no par value, $1 stated value 3,000,000 shares authorized 2,084,707 shares issued and outstanding	1,850,802
Shareholders' deficit	
Common stock, no par value 50,000,000 shares authorized 21,649,520 shares issued and outstanding	4,925,845
Common stock committed	636,424
Deferred compensation	(936,174)
Accumulated deficit	(6,397,897)
Total shareholders' deficit	(1,771,802)
Total liabilities and shareholders' deficit	$ 1,020,388

The accompanying notes are an integral part of these financial statements.

NUTRASTAR INCORPORATED AND SUBSIDIARIES
CONDENSED, CONSOLIDATED STATEMENTS OF OPERATIONS
For the Three Months Ended March 31,

	2002	2001
	(unaudited) (restated)	(unaudited)
Net sales	$ 294,357	$ 468,320
Cost of goods sold	182,472	404,425
Gross profit	111,885	63,895
Operating expenses	1,181,468	419,993
Loss from operations	(1,069,583)	(356,098)
Other income (expense)		
Interest income	600	769
Interest expense	(740)	(4,898)
Total other income (expense)	(140)	(4,129)
Net loss	$ (1,069,723)	$ (360,227)
Basic and diluted loss per share	$ (0.05)	$ (0.02)
Basic and diluted weighted-average shares outstanding	21,649,520	15,346,340

The accompanying notes are an integral part of these financial statements.

NUTRASTAR INCORPORATED AND SUBSIDIARIES

CONDENSED, CONSOLIDATED STATEMENTS OF CASH FLOWS
For the Three Months Ended March 31,

	2002	2001
	(unaudited) (restated)	(unaudited)
Cash flows from operating activities		
Net loss	$(1,069,723)	$ (360,227)
Adjustments to reconcile net loss to net cash used in operating activities		
Depreciation and amortization	29,982	16,910
Non-cash issuances of stock options	342,702	--
Non-cash issuances of committed stock	137,250	--
(Increase) decrease in		
Accounts receivable	(32,892)	21,071
Inventory	(100,080)	261,311
Prepaid expenses	(13,873)	3,977
Deposits	44,576	100,000
Increase (decrease) in		
Accounts payable	142,280	(234,011)
Accrued salaries and benefits	27,563	5,247
Accrued expenses	(1,715)	3,986
Due to officer	(19,270)	--
Net cash used in operating activities	(513,200)	(181,736)
Cash flows from investing activities		
Purchase of property and equipment	(41,124)	(179,975)
Purchase of patents and trademarks	(7,558)	(2,940)
Net cash used in investing activities	(48,682)	(182,915)
Cash flows from financing activities		
Proceeds from the issuance of common stock committed	100,000	--
Proceeds from notes payable	--	406,356
Proceeds from the issuance of common stock	--	31,000
Proceeds from note payable to officer	100,000	--
Net cash provided by financing activities	200,000	437,356
Net increase (decrease) in cash	(361,882)	72,705
Cash, beginning of year	405,502	5,865
Cash, end of year	$ 43,620	$ 78,570

The accompanying notes are an integral part of these financial statements.

NUTRASTAR INCORPORATED AND SUBSIDIARIES
CONDENSED, CONSOLIDATED STATEMENTS OF CASH FLOWS
For the Three Months Ended March 31,

	2002 (unaudited) (restated)	2001 (unaudited)
Supplemental disclosures of cash flow information		
Interest paid	$ --	$ --
Income taxes paid	$ 1,600	$ --

The accompanying notes are an integral part of these financial statements.

NUTRASTAR INCORPORATED AND SUBSIDIARIES
NOTES TO CONDENSED, CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2002 (unaudited)

NOTE 1 - ORGANIZATION AND LINE OF BUSINESS

General

NutraStar Incorporated ('NutraStar"), a California corporation, markets proprietary whole food dietary supplements derived from nutrient-dense stabilized rice bran (a nutraceutical) produced by an affiliated company, The RiceX Company ("RiceX"), a current shareholder and a publicly traded company. The Company has a license to distribute certain derivatives of RiceX's stabilized rice bran, as well as valued-added rice bran products in the United States of America.

On December 14, 2001, Alliance Consumer International, Inc. ("Alliance") acquired all of the outstanding common stock of NutraStar. For accounting purposes, the acquisition has been treated as a recapitalization of NutraStar with NutraStar as the acquirer (reverse acquisition).

Effective April 27, 2000, NutraStar became an 80% owner of NutraGlo Incorporated ("NutraGlo"), a Nevada corporation. NutraGlo was non-operative during 2000. During the year ended December 31, 2002, NutraGlo started marketing, manufacturing, and distributing NutraStar's stabilized rice bran and other nutraceuticals to the equine market. In connection with NutraStar's acquisition of Alliance, NutraStar issued 250,001 shares of common stock in exchange for the remaining 20% of the common stock of NutraGlo. The value of the shares was $250,001, which has been recorded as goodwill in the accompanying consolidated balance sheet.

NOTE 2 - RESTATEMENT

During the year ended December 31, 2001, the Company issued 130,000 shares of Series A preferred stock to a related party as payment of accounts payable totaling $130,000. Related to these issuances, on January 15, 2002, these holders executed a put/call agreement with the Company (see Note 7). The Company previously had not recorded the put option on its financial statements. The Company has also reclassified its convertible Series A preferred stock to convertible, redeemable Series A preferred stock to conform with the accounting requirements of the United States Securities and Exchange Commission.

This restatement does not have any effect on the Company's reported earnings. Its impact on the previously reported total liabilities and convertible, redeemable Series A preferred stock as of March 31, 2002 are as follows:

	As Previously Reported	Restatement	As Restated
Total liabilities	$ 811,388	$ 130,000	$ 941,388
Total convertible, redeemable Series A preferred stock	$ 1,980,802	$ (130,000)	$ 1,850,802

NOTE 3 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation

The consolidated financial statements include the accounts of NutraStar and its wholly owned subsidiaries, NutraStar Technologies, Inc. and NutraGlo (collectively, the "Company"). All significant inter-company accounts and transactions are eliminated in consolidation.

Basis of Presentation

The accompanying financial statements have been prepared in conformity with generally accepted accounting principles for interim financial information and with the instructions to Form 10-QSB and Regulation S-B. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all normal, recurring adjustments considered necessary for a fair presentation have been included. The financial statements should be read in conjunction with the audited financial statements and notes thereto included in the Company's Annual Report on Form 10-KSB for the year ended December 31, 2001. The results of operations for the three months ended March 31, 2002 are not necessarily indicative of the results that may be expected for the year ended December 31, 2002.

Going Concern

The Company has received a report from its independent auditors that includes an explanatory paragraph describing the uncertainty as to the Company's ability to continue as a going concern. These consolidated financial statements contemplate the ability to continue as such and do not include any adjustments that might result from this uncertainty.

Advertising Expense

The Company expenses all advertising costs, including direct response advertising, as they are incurred. Advertising expense for the three months ended March 31, 2002 and 2001 was $20,346 (unaudited) and $7,326 (unaudited), respectively.

Estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Reclassifications

Certain amounts included in the prior period financial statements have been reclassified to conform with the current period presentation. Such reclassification did not have any effect on reported net loss.

NOTE 3 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Recently Issued Accounting Pronouncement

In April 2002, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 145, "Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections." SFAS No. 145 updates, clarifies, and simplifies existing accounting pronouncements. This statement rescinds SFAS No. 4, which required all gains and losses from extinguishment of debt to be aggregated and, if material, classified as an extraordinary item, net of related income tax effect. As a result, the criteria in Accounting Principles Board No. 30 will now be used to classify those gains and losses. SFAS No. 64 amended SFAS No. 4 and is no longer necessary as SFAS No. 4 has been rescinded. SFAS No. 44 has been rescinded as it is no longer necessary. SFAS No. 145 amends SFAS No. 13 to require that certain lease modifications that have economic effects similar to sale-leaseback transactions be accounted for in the same manner as sale-lease transactions. This statement also makes technical corrections to existing pronouncements. While those corrections are not substantive in nature, in some instances, they may change accounting practice. The Company does not expect adoption of SFAS No. 145 to have a material impact, if any, on its financial position or results of operations.

NOTE 4 - PROPERTY AND EQUIPMENT

Property and equipment at March 31, 2002 consisted of the following:

Furniture and equipment	$ 18,417
Software	327,747
	346,164
Less accumulated depreciation	121,031
Total	$225,133

Depreciation expense was $26,946 (unaudited) and $15,604 (unaudited) for the three months ended March 31, 2002 and 2001, respectively.

NUTRASTAR INCORPORATED AND SUBSIDIARIES
NOTES TO CONDENSED, CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2002 (unaudited)

NOTE 5 - PATENTS AND TRADEMARKS

Patents and trademarks at March 31, 2002 consisted of the following:

Patents	$ 72,738
Trademarks	51,809
	124,547
Less accumulated amortization	10,520
Total	$114,027

Amortization expense was $3,036 (unaudited) and $1,306 (unaudited) for the three months ended March 31, 2002 and 2001, respectively.

NOTE 6 - NOTE PAYABLE TO OFFICER

On March 4, 2002, the Company entered into a note payable agreement with an officer of the Company, which bears interest at 10% per annum and is due on March 3, 2003.

NOTE 7 - PUT OPTION

During the year ended December 31, 2001, the Company issued 130,000 shares of Series A preferred stock to a related party as payment of accounts payable totaling $130,000. On January 15, 2002, these holders of the Series A preferred stock executed a put/call agreement. The put allows for the holder to sell to the Company all, but not less than all, of the 130,000 shares of the Company's Series A preferred stock, or common stock if any of the Series A preferred stock were converted, for $130,000, plus all accumulated, but unpaid dividends, at any time after six months from January 15, 2002. Related to the put option and the related conversion of debt, the Company has recorded a liability of $130,000.

In addition, the Company maintains the right to call the option and purchase back the shares of the Series A preferred stock for $130,000, plus any unpaid and accrued dividends at any time, subject to certain provisions.

NOTE 8 - CONTINGENCIES

Litigation

The Company is involved in certain legal proceedings and claims which arise in the normal course of business. Management does not believe that the outcome of these matters will have a material effect on the Company's financial position or results of operations.

NOTE 9 - SHAREHOLDERS' DEFICIT

Common Stock Committed

On March 15, 2002, the Company committed to issue 153,333 shares of common stock with a detachable purchase warrant to purchase 153,333 shares of common stock at an exercise price of $1.20 per share in exchange for $100,000. As of March 31, 2002, the Company had not issued the stock and has recorded the transaction as committed stock.

Common Stock and Stock Options

On January 7, 2002, the Company entered into a five-year employment agreement with an employee. In relation to this agreement, the Company issued options to purchase 155,000 shares of common stock. The options vest over four years in increments of 80,000, 25,000, 25,000, and 25,000, have an exercise price of $1 per share, and expire on January 7, 2012. As of March 31, 2002, the Company recorded compensation expense and deferred compensation totaling $48,438 and $145,312, respectively, in relation to this transaction.

On January 10, 2002, the Company entered into a six-month consulting services agreement for marketing services. In relation to this agreement, the Company issued options to purchase 25,000 shares of common stock at an exercise price of $1 per share. The options expire in 10 years. The Company recorded consulting expense of $47,250 in relation to this transaction.

On February 4, 2002, the Company entered into a three-month marketing services agreement for public relations and advertising services. In relation to this agreement, the Company paid a retainer of $35,000 upon execution of the agreement, issued 35,000 shares of restricted common stock, and issued options to purchase 50,000 shares of the Company's common stock at an exercise price of $3 per share. The options expire in two years. The Company recorded consulting expense totaling $90,250 in relation to this transaction.

NOTE 9 - SHAREHOLDERS' DEFICIT (Continued)

Common Stock and Stock Options (Continued)

On February 21, 2002, the Company entered into a one-year financial advisory services agreement. In relation to this agreement, the Company paid a non-refundable retainer of $20,000, issued 200,000 restricted shares of common stock, and issued options to purchase 100,000 restricted shares of common stock at $1 per share, 100,000 at $2.50 per share, and 100,000 at $4 per share. The Company recorded consulting expense totaling $159,000 in relation to this transaction.

NOTE 10 - SUBSEQUENT EVENTS

On April 12, 2002, the Company entered into a two-year marketing agreement, whereby the Company is to pay a commission of 10% of gross receipts on sales from customers introduced to the Company by the consultant, subject to certain requirements. In relation to this agreement, the Company granted to the consultants five-year options to purchase up to 150,000 shares of the Company's common stock at an exercise price of $0.75 per share, vesting according to the achievement of certain levels of gross receipts. The agreement automatically renews after the initial two-year term.

On May 6, 2002, the Company entered into a one-year finder's and advisory agreement, whereby the finder is to seek businesses that are consistent with the Company's business and strategic plans or to introduce the Company to investors. The fees paid to the finder for finding investors to fund the Company are based upon certain percentages, ranging from 2% to 10%, plus unaccountable expenses, depending on the amount funded by the investors. In addition, 10% of the transaction value will be paid in cashless warrants. If the finder arranges a credit line or other types of debt placement, the fees paid to the finder will be 2% of the total debt placement. If the finder introduces a business or entity and the Company engages in a merge-type transaction or other similar transactions, the fees paid to the finder are based upon certain percentages, ranging from 3% to 7%, depending on the transaction value. In addition, 10% of the transaction value will be paid in cashless warrants. This agreement is automatically renewed after the initial one-year term.

ITEM 2. MANAGEMENT'S DISCUSSIONS AND ANALYSIS OR PLAN OF OPERATIONS

Caution About Forward-Looking Statements

This Form 10-QSB includes "forward-looking" statements about future financial results, future business changes and other events that haven't yet occurred. For example, statements like we "expect," we "anticipate" or we "believe" are forward-looking statements. Investors should be aware that actual results may differ materially from our expressed expectations because of risks and uncertainties about the future. The Company does not undertake to update the information in this Form 10-QSB if any forward-looking statement later turns out to be inaccurate. Details about risks affecting various aspects of the Company's business are discussed throughout this Form 10-QSB and should be considered carefully.

Plan of Operation for the Next Twelve Months

NTI was formed on February 4, 2000 and became the wholly-owned subsidiary of the Company on December 14, 2001. To date, the Company has focused on its relationship with the producer of its raw materials, RiceX, and to a lesser extent on its strategic alliances. The Company has commenced the limited distribution of its stabilized rice bran and rice bran products on the Internet and through direct-to-consumer response advertising campaigns. In the near future, the Company intends to commence the full distribution of its products as private label brands through strategic distributors on the occurrence of certain events, including the raising of additional capital required to implement the Company business plan.

The Company anticipates that in the next 12 to 24 months, it will need an additional $10 to $20 million in financing. The Company anticipates that it will need $5 to $15 million to make certain acquisitions, $2.5 million to further increase production capacity, and $2.5 million for additional working capital, including the purchase of inventory for anticipated sales growth. The Company expects to obtain this additional funding from private placements of debt and/or equity securities, or possibly through the public offering of its common stock.

Results of Operation

First Quarter 2002 versus First Quarter 2001

During the first quarter 2002, NutraStar generated net sales of $294,357 compared to $468,320 for the first quarter 2001, a decrease of 37% in comparison to 2001. Reasons for the decrease include a delay in obtaining final approval of the new Exclusive Distribution Agreement with The RiceX Company, which temporarily limited the amount of stabilized rice bran being shipped to the Company. In addition, new terms of the Exclusive Distribution Agreement transferred prior industrial customers of NutraStar to RiceX.

The cost of goods sold for the quarter ended March 31, 2002 decreased 45% to $182,472 compared to $404,425 for the quarter ended March 31, 2001. This decrease reflects the increase in production of higher margin products for resale as well as 2001 having more start-up production costs. The Company's gross profit percentage increased to 38% from 14% for the quarter ended March 31, 2002 compared to the quarter ended March 31, 2001. Operating expenses of

$1,181,468 in the first quarter of 2002 more than doubled over the comparable period in fiscal year 2001 with operating expenses of $419,993. This increase represents the Company's continued expansion of operations during fiscal year 2002 in a number of areas. During the quarter ended March 31, 2002 employee related expenses rose $235,000 to $451,000 as result of additional hired employees both after the first quarter of 2001 and during the first quarter of 2002. Professional fees increased approximately $449,000 to $558,000 in the first quarter of 2002 as the Company is using outside consultants in such areas as legal, financial and marketing in an attempt to limit direct hires until additional funding is obtained. Included in operating expenses in the quarter-ended March 31, 2002 is approximately $479,951 related to restricted stock grants issued in lieu of cash to both employees and outside consultants.

The Company incurred an operating loss of $1,069,583 during the quarter ended March 31, 2002 compared to an operating loss of $356,098 during the quarter ended March 31, 2001. This 200% increase in operating loss reflects the significant increase in the operating expenses relating to the Company's expanded business operations during fiscal year 2002 as discussed above.

During the quarter ended March 31, 2002, the Company recognized interest expense of $740, which reflects interest paid on short-term promissory notes outstanding during all or part of the quarter and represents a decrease from interest expense of $4,898 for the quarter ended March 31, 2001 which reflects the significant reduction in the amount of promissory notes outstanding. This expense increased the Company's overall net loss to $1,069,723 compared to a total loss of $360,227 recorded in the quarter ended March 31, 2001.

Due to the December 14, 2001 share exchange with Alliance, for accounting purposes, the acquisition has been treated as a recapitalization of NutraStar (formerly Alliance) with NTI as the acquirer (reverse acquisition). Consequently, the financial statements of NTI are presented as those of the Company. As a result, a comparison of the current financial statements as compared to those of Alliance as previously reported in its Form 10-SB may not be deemed relevant.

Liquidity and Sources of Capital

NutraStar has incurred significant operating losses since its inception, and, as of March 31, 2002 NutraStar has an accumulated deficit of $6,397,897. At March 31, 2002, NutraStar had cash and cash equivalents of $43,620 and a net working capital deficit of $516,656.

To date, NutraStar has funded its operations, in addition to sales revenues, through a combination of short-term debt and the issuance of common and preferred stock. As of December 31, 2000 NutraStar had raised approximately $383,000 from the sale of its common stock through private placement channels. During December 2001 NutraStar completed two private placements; the first raised $1,000,000 from the sale of common stock at $1.00 per share; and the second raised approximately $1,841,707 through the conversion of debt and accrued interest into preferred stock that was priced at $1.00 per share, which is classified as convertible, redeemable Series A Preferred Stock to conform with SEC accounting requirements. During the quarter ended March 31, 2002, NutraStar raised an additional $100,000 through the sale of its common stock as well as received proceeds of $100,000 from a note payable to the Chairperson of NutraStar.

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The Company expects its expenses to continue to increase during the foreseeable future as a result of increased marketing expenses and expansion of its product line. The Company is dependent on the proceeds from future debt or equity investments to expand its operations and fully implement the Company's business plan. If the Company is unable to raise sufficient capital, the Company will be required to delay or forego some portion of its business plan, which may have a material adverse effect on the Company's anticipated results from operations and financial condition. Alternatively, the Company may seek interim financing in the form of bank loans, private placement of debt or equity securities, or some combination thereof. Such interim financing may not be available in the amounts or at the times when the Company requires, and will likely not be on terms favorable to the Company.

Dependence on Key Supplier

NutraStar has entered into an agreement with The RiceX Company, whereby RiceX will sell NutraStar its rice bran solubles and rice bran fiber concentrates at prices equal to the lower of RiceX's standard price or the price negotiated by other customers for like quantities and products. The agreement also provides that RiceX will not sell any rice bran solubles or rice bran fiber concentrates products in the United States except to NutraStar. To maintain this exclusive right, NutraStar must purchase products equal to $250,000 by April 15, 2002 (which quota has been met), $500,000 during the three-month period ending July 15, 2002, $750,000 during the three-month period ending October 15, 2002, $1,250,000 during the three-month period ending January 15, 2003, $1,500,000 for the six month period ending July 15, 2003, $2,250,000 for the six-month period ending January 15, 2004, $6,000,000 for the one-year period ending January 15, 2005, and increasing amounts each one-year period thereafter at a 10% increase per year. In consideration for this exclusive right, NutraStar will pay RiceX a royalty of 2% of NutraStar's gross receipts of all NutraStar's products that incorporated RiceX products, exclusive of shipping charges and returned product. To purchase products from RiceX, the NTI is required to provide a 50% deposit for all purchase orders in addition to the $135,000 security deposit already paid to RiceX. The agreement has a 5-year term, and automatically renews for 2 additional 5-year terms unless NutraStar elects not to renew.

In addition to the risks associated with the potential termination of the RiceX Agreement, the inability of RiceX to deliver the amount of product that NutraStar requires, any interruption in product delivery for any reason, or the inability of RiceX to fulfill its contractual obligations would have a material adverse effect on NutraStar's business, results from operations, and financial condition, as NutraStar could not readily find and implement alternative suppliers and likely not on advantageous terms. NutraStar has the exclusive right to distribute certain of RiceX's products in the United States, but NutraStar may lose this exclusive right if it does not purchase increasing amounts of product from RiceX each year. RiceX's ability to manufacture certain of NutraStar's core products is currently limited to the production capability of RiceX's Dillon, Montana plant (the "Dillon Plant"). Currently, the Dillon Plant is capable of producing only a limited quantity of NutraStar's products, which will not be sufficient to meet NutraStar's short-term and long-term sales goals. The Company and/or RiceX plan to add production capacity during the current year.

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Recently Issued Accounting Pronouncements

In June 2001, the Financial Accounting Standards Board ("FASB") issued SFAS No. 141, "Business Combinations." This statement addresses financial accounting and reporting for business combinations and supersedes APB Opinion No. 16, "Business Combinations," and SFAS No. 38, "Accounting for Pre-Acquisition Contingencies of Purchased Enterprises." All business combinations in the scope of this statement are to be accounted for using one method, the purchase method. The provisions of this statement apply to all business combinations initiated after June 30, 2001.

Use of the pooling-of-interests method for those business combinations is prohibited. This statement also applies to all business combinations accounted for using the purchase method for which the date of acquisition is July 1, 2001 or later. NutraStar does not expect adoption of SFAS No. 141 to have a material impact, if any, on its financial position or results of operations.

In June 2001, the FASB issued SFAS No. 142, "Goodwill and Other Intangible Assets." This statement addresses financial accounting and reporting for acquired goodwill and other intangible assets and supersedes APB Opinion No. 17, "Intangible Assets." It addresses how intangible assets that are acquired individually or with a group of other assets (but not those acquired in a business combination) should be accounted for in financial statements upon their acquisition. This statement also addresses how goodwill and other intangible assets should be accounted for after they have been initially recognized in the financial statements. It is effective for fiscal years beginning after December 15, 2001. Early application is permitted for entities with fiscal years beginning after March 15, 2001, provided that the first interim financial statements have not been issued previously. NutraStar does not expect adoption of SFAS No. 142 to have a material impact, if any, on its financial position or results of operations.

In June 2001, the FASB issued SFAS No. 143, "Accounting for Asset Retirement Obligations." This statement applies to legal obligations associated with the retirement of long-lived assets that result from the acquisition, construction, development, and/or the normal operation of long-lived assets, except for certain obligations of lessees. This statement is not applicable to NutraStar.

In August 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." This statement addresses financial accounting and reporting for the impairment or disposal of long-lived assets. This statement replaces SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed of," the accounting and reporting provisions of APB No. 30, "Reporting the Results of Operations - Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual, and Infrequently Occurring Events and Transactions," for the disposal of a segment of a business, and amends Accounting Research Bulletin No. 51, "Financial Statements," to eliminate the exception to consolidation for a subsidiary for which control is likely to be temporary. NutraStar does not expect adoption of SFAS No. 144 to have a material impact, if any, on its financial position or results of operations.

Critical Accounting Policies

Our discussion and analysis of our financial conditions and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with generally accepted accounting principles in the

United States. The preparation of financial statements require managers to make estimates and judgments that affect the reported amounts of assets and liabilities, revenues and expenses and disclosures on the date of the financial statements. On an on-going basis, we evaluate our estimates, including, but not limited to, those related to revenue recognition. We use authoritative pronouncements, historical experience and other assumptions as the basis for making judgments. Actual results could differ from those estimates. We believe that the following critical accounting policies affect our more significant judgments and estimates in the preparation of our consolidated financial statements.

Revenue recognition

We are required to make judgments based on historical experience and future expectations, as to the realizability of shipments made to our customers. These judgments are required to assess the propriety of the recognition of revenue based on Staff Accounting Bulletin ("SAB") No. 101, "Revenue Recognition," and related guidance. We make these assessments based on the following factors: i) customer-specific information, ii) return policies, and iii) historical experience for issues not yet identified.

Valuation of long-lived assets

Long-lived assets, consisting primarily of property and equipment, patents and trademarks, and goodwill, comprise a significant portion of NutraStar's total assets. Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that their carrying values may not be recoverable. Recoverability of assets is measured by a comparison of the carrying value of an asset to the future net cash flows expected to be generated by those assets. The cash flow projections are based on historical experience, management's view of growth rates within the industry, and the anticipated future economic environment.

Factors we consider important that could trigger a review for impairment include the following:

(a) significant underperformance relative to expected historical or projected future operating results,

(b) significant changes in the manner of our use of the acquired assets or the strategy of our overall business, and

(c) significant negative industry or economic trends.

When we determine that the carrying value of patents and trademarks, long-lived assets and related goodwill and enterprise-level goodwill may not be recoverable based upon the existence of one or more of the above indicators of impairment, we measure any impairment based on a projected discounted cash flow method using a discount rate determined by our management to be commensurate with the risk inherent in our current business model.

PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

Subsequent to the quarter ended March 31, 2002, a Complaint was filed against NTI by Millennium Integrated Services, Inc. ("MISI") in Superior Court, Sacramento County, on April 4, 2002 (Case No. 02A502006). MISI provided website development services to NTI, at a cost of $204,405. MISI is seeking contract payment of $204,405 plus interest of $32,031 as well as damages for alleged conversion and misappropriation of trade secrets. Additionally, MISI has stated that it will move the court to amend its Complaint to add a cause of action for negligent and intentional interference with an employment agreement between MISI and one of its programmers. On April 9, 2002, MISI filed a Motion for a Writ of Attachment which would allow MISI to seize and hold NTI assets worth $236,436 pending the resolution of the lawsuit. On April 10, 2002, a Writ of Attachment was granted by the Court. NTI believes it has valid defenses and offsets to the payment for these services and either will appeal the Court's action or attempt to settle this matter. Discovery is just beginning and it is too early to opine upon the possible outcome of the litigation. Settlement of this case could have a material affect on NutraStar's cash flow depending on how quickly any settlement would need to be paid. Conversely, litigating this matter could also have a material adverse affect on NutraStar's operations and financial results.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits: None

(b) Reports on Form 8-K:

On February 27, 2002, the Company filed an Amended Form 8-K/A for December 14, 2002, reporting an Item 7 submission regarding the filing of financial statements resulting from the Company's Plan and Agreement of Exchange with NTI.

On March 14, 2002, the Company filed a Form 8-K for March 7, 2002, reporting an Item 4 event regarding the change of independent accountants for the Company and its subsidiaries.

On March 25, 2002, the Company filed an Amended Form 8-K/A for March 7, 2002, revising the Item 4 information previously filed and including additional exhibits under Item 7.

SIGNATURES

In accordance with the requirements 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.

NUTRASTAR INCORPORATED

Dated: June 5, 2002

By: /s/ James Kluber

James Kluber
Chief Financial Officer
(Principal Accounting Officer)