NUTRASTAR INC
Form 10QSB
May 20, 2003

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-QSB

[X] QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934
FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2003

[ ] 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, 25,598,547 issued and outstanding as of May 16, 2003.

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PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

NUTRASTAR INCORPORATED AND SUBSIDIARIES
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NUTRASTAR INCORPORATED AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEET
March 31, 2003 (unaudited)

ASSETS

Current assets	
Cash	$ 37,982
Accounts receivable	123,091
Inventory	30,271
Prepaid expenses	5,417
Total current assets	196,761
Property and equipment, net	125,857
Patents and trademarks, net	48,789
Goodwill	250,001
Total assets	$621,408

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NUTRASTAR INCORPORATED AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEET
March 31, 2003 (unaudited)

LIABILITIES AND SHAREHOLDERS' DEFICIT

Current liabilities	
Accounts payable	$ 730,942
Accrued salaries and benefits	127,978
Deferred compensation	438,846
Accrued expenses	37,862
Customer deposits	50,112
Due to officer	19,517
Due to related party	26,772
Notes payable - related party	336,222
Note payable	50,000

Total current liabilities	1,818,251
Put option	130,000
Total liabilities	1,948,251
Commitments and contingencies	
Convertible, redeemable series A preferred stock, no par value, $1 stated value 3,000,000 shares authorized 2,144,707 (unaudited) shares issued and outstanding	2,098,463
Shareholders' deficit	
Common stock, no par value 50,000,000 shares authorized 24,791,404 (unaudited) shares issued and outstanding	5,540,796
Committed common stock	571,674
Deferred compensation	(840,197)
Accumulated deficit	(8,697,579)
Total shareholders' deficit	(3,425,306)
Total liabilities and shareholders' deficit	$ 621,408

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

	2003	2002
	(unaudited)	(unaudited)
Net sales	$ 225,991	$ 294,357
Cost of goods sold	127,399	182,472
Gross profit	98,592	111,885
Operating expenses	462,607	1,181,468
Loss from operations	(364,015)	(1,069,583)
Other income (expense)		

Interest income	--	600
Interest expense	(17,191)	(740)
Total other income (expense)	(17,191)	(140)
Net loss	(381,206)	(1,069,723)
Cumulative preferred dividends	37,532	--
Net loss attributable to common shareholders	$ (418,738)	$ (1,069,723)
Basic and diluted loss attributable to common shareholders per common share	$ (0.02)	$ (0.05)
Weighted-average number of common shares used to compute basic and diluted loss attributable to common shareholders per share	24,190,849	21,649,520

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

	2003	2002
	(unaudited)	(unaudited)
Cash flows from operating activities		
Net loss	$ (381,206)	$(1,069,723)
Adjustments to reconcile net loss to net cash used in operating activities		
Depreciation and amortization	32,297	29,982
Non-cash issuances of committed stock	--	137,250
Non-cash issuances of stock options	--	342,702
Amortization of deferred compensation	33,076	--
(Increase) decrease in		
Accounts receivable	(115,818)	(32,892)
Inventory	12,424	(100,080)
Prepaid expenses	21,763	(13,873)
Deposits	--	44,576

Increase (decrease) in		
Accounts payable	16,611	142,280
Accrued salaries and benefits	24,392	27,563
Deferred compensation	112,884	--
Accrued expenses	8,800	(1,715)
Customer deposits	5,796	--
Due to officer	(7,077)	(19,270)
Due to related party	(3,617)	--
Net cash used in operating activities	(239,675)	(513,200)
Cash flows from investing activities		
Purchase of property and equipment	--	(41,124)
Purchase of patents and trademarks	(2,483)	(7,558)
Net cash used in investing activities	(2,483)	(48,682)
Cash flows from financing activities		
Proceeds from notes payable - related party	240,422	100,000
Principal payments on notes payable - related party	(85,000)	--
Proceeds from the issuance of common stock	90,000	--
Proceeds from the issuance of committed common stock	--	100,000

Net cash provided by financing activities	245,422	200,000
Net increase (decrease) in cash	$ 3,264	$ (361,882)
Cash, beginning of period	34,718	405,502
Cash, end of period	$ 37,982	$ 43,620
Supplemental disclosures of cash flow information		
Interest paid	--	--

Income taxes paid	--	$ 1,600

NUTRASTAR INCORPORATED AND SUBSIDIARIES
NOTES TO CONDENSED, CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2003 (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 (as defined in Note 2) 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, 2001, 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 transaction has been accounted for in accordance with Statement of Financial Accounting Standards ("SFAS") No. 141, "Business Combinations," which is required for all transactions occurring after June 30, 2001. In accordance with SFAS No. 141, the purchase price is to be allocated to assets acquired and liabilities assumed based on the estimated fair market value at the closing date of the acquisition, with the excess of the purchase price being allocated to goodwill. Since there were not any assets acquired and liabilities assumed in connection with this transaction, the value of the shares issued of $250,001 has been recorded as goodwill in the accompanying consolidated balance sheet. As NutraStar was the 80% owner of NutraGlo, the operations of NutraGlo have been consolidated with NutraStar. Therefore, pro forma information is not required.

Lines of Business

The Company has four primary divisions through which it sells its products: (1) TheraFoods(R), which distributes consumer products including RiSolubles(R), RiceMucil(R), NutraFlex(TM), and StaBran(R), (2) NutraCea(R), which was created to compliment medical food products, (3) NutraBeauticals(R), which provides natural products to improve skin health, and (4) NutraGlo(R), which developed a derivative of the NutraFlex(TM) product for horses.

For internal reporting purposes, management segregates the Company into two segments: (1) NutraStar, including the transactions of TheraFoods(R), NutraCea(R), and NutraBeauticals(R), and (2) NutraGlo(R).

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation

The consolidated financial statements include the accounts of NutraStar and its wholly owned subsidiaries, NutraStar Technologies Incorporated and NutraGlo(R) (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 accounting principles generally accepted in the United States of America 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 accounting principles generally accepted in the United States of America 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, 2002. The results of operations for the three months ended March 31, 2003 are not necessarily indicative of the results that may be expected for the year ended December 31, 2003.

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.

Revenue Recognition

Revenue is generally recognized upon shipment of product with a provision for estimated returns and allowances recorded at that time, if applicable. Commissions revenue is generally recognized when earned and collection is reasonably assured.

Deferred Compensation

Deferred compensation at March 31, 2003 consisted of salaries payable to employees of the Company that have been earned, but not paid.

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, 2003 and 2002 was $1,973 and $20,346, respectively.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

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 reclassifications did not have any effect on reported net loss.

Concentrations of Credit Risk

The Company sells its services throughout the United States, extends credit to its customers, and performs ongoing credit evaluations of such customers. The Company evaluates its accounts receivable on a regular basis for collectibility and provides for an allowance for potential credit losses as deemed necessary.

On May 1, 2001, the Company entered into a three-year, exclusive distribution agreement with a customer, in which the customer is required to purchase a minimum of 90,000 pounds of the Company's product on or before July 1, 2001, 120,000 pounds before September 1, 2002, 275,000 pounds between September 1, 2002 and August 31, 2003, and 350,000 pounds between September 1, 2003 and August 31, 2004. During the three months ended March 31, 2003, sales to this customer totaled $203,574 (90% of net sales). During the three months ended March 31, 2002, sales to this customer totaled $153,546 (52% of net sales).

NOTE 3 - PROPERTY AND EQUIPMENT

Property and equipment at March 31, 2003 consisted of the following:

Furniture and equipment	$	18,417
Software		347,773
		366,190
Less accumulated depreciation		240,333
Total	$	125,857

Depreciation expense was $29,855 and $26,946 for the three months ended March 31, 2003 and 2002, respectively.

NOTE 4 - PATENTS AND TRADEMARKS

Patents and trademarks at March 31, 2003 consisted of the following:

Patents	$	91,882
Trademarks		52,259
		144,141
Less loss reserve		75,359
Less accumulated amortization		19,993
Total	$	48,789

At March 31, 2003, $505 of the Company's patents and trademarks had been purchased from a related party.

The Company recorded a loss reserve totaling $75,359 as of March 31, 2003 related to the impairment of certain patents.

Amortization expense was $2,442 and $3,036 for the three months ended March 31, 2003 and 2002, respectively. Future estimated, aggregate amortization expense at March 31, 2003 was as follows:

12 Months Ended March 31,		
2004	$	9,696

2005	9,696
2006	9,696
2007	9,696
Total	$ 38,784

NOTE 5 - GOODWILL

Goodwill represents the purchase price of the remaining 20% of NutraGlo. As of January 1, 2002, the Company adopted SFAS No. 142. SFAS No. 142 prohibits the amortization of goodwill, but requires that it be reviewed for impairment at least annually or on an interim basis if an event occurs or circumstances change that could indicate that its value has diminished or been impaired. Recoverability of goodwill is measured by a comparison of its carrying value to the future net cash flows expected to be generated by it.

NOTE 5 - GOODWILL (Continued)

Cash flow projections are based on historical experience, management's view of growth within the industry, and the anticipated future economic environment. Since the Company purchased the remaining 20% of NutraGlo on December 12, 2001, amortization expense was not recorded as of December 31, 2001. As such, the transitional disclosure provisions of SFAS No. 142 do not apply.

NOTE 6 - NOTES PAYABLE - RELATED PARTIES

Notes payable - related parties at March 31, 2003 consisted of the following:

Notes payable to the Chief Executive Officer, bearing interest at 10% per annum and due on demand.	$ 201,222
Notes payable to a related party, bearing interest at 8% per annum, collateralized by all of the assets of the Company, and due on May 6, 2003.	90,000
Notepayable to a related party, bearing interest at 2% per month, collateralized by 400,000 shares of the Company's common stock, and due on June 3, 2003.	40,000
Notepayable to a related party, bearing interest at 2% per month, collateralized by 50,000 shares of the Company's common stock, and due on June 8, 2003.	5,000

Total	$ 336,222

NOTE 7 - NOTE PAYABLE

The note payable at March 31, 2003 amounted to $50,000 to a third party, bearing interest at 2% per month, secured by 634,121 shares of preferred stock, and due on September 20, 2003.

NOTE 8 - 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 9 - COMMITMENTS AND CONTINGENCIES

Registration Statement

The Company will pay all of the costs connected with the registration on Form SB-2 related to the re-sale of up to 3,709,028 shares of common stock originally filed on June 4, 2002, except the holder of the common stock will pay all sales commissions or brokers' discounts and the fees and expenses of the holders' legal counsel or accountants, if any.

Consulting Agreement

On March 5, 2003, the Company entered into a consulting agreement for certain consulting services. As compensation for any funding, the consultants are to be paid 7.5% of any cash received, 2.5% in value of such funding in common stock of the Company, based on the closing price on the day any agreement is signed, and a warrant to purchase one share of the Company's common stock for every dollar funded. The warrants are exercisable at $0.50 per share on or before three years from the

anniversary of any funding.

Litigation

On April 4, 2002, a complaint was filed against the Company by Millennium Integrated Services, Inc. ("MISI"). MISI provided Web site development services to the Company at a cost of $204,405. MISI is seeking contract payment of $204,405, plus interest of $32,031 and damages for alleged conversion and misappropriation of trade secrets. On April 9, 2002, MISI filed a Motion for a Writ of Attachment that would allow MISI to seize and hold the Company's assets worth $236,436, pending the resolution of the lawsuit. This Writ of Attachment was granted on April 10, 2002.

NOTE 9 - COMMITMENTS AND CONTINGENCIES (Continued)

Litigation (Continued)

Certain of the Company's accounts receivable as of March 31, 2003 have been attached to secure an accounts payable balance to MISI of $186,666 as of March 31, 2003. Management believes that the settlement of this case may have a material effect on the Company's cash flows, but is unable to quantify such effect at this time.

On July 16, 2002, the Company was summoned to answer a complaint filed by Faraday Financial, Inc. ("Faraday"). Between December 2000 and March 2001, the Company issued convertible promissory notes totaling $450,000 and a promissory note totaling $50,000. On December 13, 2001, Faraday entered into a settlement agreement with the Company, whereby Faraday agreed to cancel the promissory notes in exchange for 735,730 shares of preferred stock. Faraday claims that the settlement agreement required that the Company effect a registration statement covering the preferred stock by June 30, 2002. In the event the Company failed to effect a registration statement by June 30, 2002, the Company was to immediately forfeit to Faraday 735,730 shares of common stock in the name of the Chief Executive Officer of the Company.

In addition, the Chief Executive Officer entered into an escrow agreement to ensure the automatic forfeiture of the common stock and entered into a guarantee to be personally responsible to Faraday for the original $500,000 loan amount, plus 12% interest per annum. As of March 31, 2003, management believes the maximum exposure for the Company is approximately $500,000, plus interest and fees.

The Company was involved in litigation with several potential investors. The plaintiffs requested a return of $750,000 in funds deposited with the Company, representing potential permanent investments. These matters have been resolved in connection with the acquisition of Alliance during December 2001. As of March 31, 2003, there were not any additional liabilities related to these matters.

There are various other claims that have been made against the Company

by certain of its vendors. Management expects that the settlement of these claims will not have a significant effect on the Company's financial position and results of operations.

From February through July 2000, a third party solicited funds on behalf of an undetermined public shell company, into which it was contemplated that the Company might merge. In this regard, the Company received approximately $320,000 in deposits to be used for such purpose. As a result of these solicitations, there may have been violations of federal and/or state securities laws by such third party. The Company never proceeded with the contemplated merger.

NOTE 9 - COMMITMENTS AND CONTINGENCIES (Continued)

Litigation (Continued)

Instead, the Company applied such funds to a subsequent private placement that the Company conducted, in which shares of the Company's common stock were issued for the $320,000 investment. The Company has offered full refunds to all people who provided monies to the Company. There are not any assurances that federal and/or state securities authorities will not investigate and possibly bring an action against the third party who solicited the funds and the Company.

NOTE 10 - SHAREHOLDERS' DEFICIT

Convertible, Redeemable Series A Preferred Stock

In December 2001, the Company approved the issuance of 3,000,000 shares of convertible, redeemable Series A preferred stock and executed a certificate of designation of the rights, preferences, and privileges of the Series A preferred stock. Each shareholder of Series A preferred stock is entitled to receive a 7% cumulative dividend, which is only payable in the case of liquidation or redemption. The Series A preferred stock has a $1 per share stated value and will receive certain liquidation preferences after satisfaction of claims of creditors, but before payment or distributions of assets and surplus funds.

Furthermore, the Series A preferred stock is convertible at the option of the holder at $1 per share into the Company's common stock, subject to certain anti-dilution provisions. In addition, the Series A preferred stock will automatically convert into common stock in the event of a qualified public trading benchmark, which is defined as (i) the common stock is listed on a national exchange at twice its conversion price or (ii) the common stock is quoted on the over-the-counter bulletin board at an average bid price of at least $1.25 per share over any 30-day trading period.

The Company may redeem any and all outstanding shares of Series A preferred stock. Upon the five-year anniversary of the date of

issuance, the Company is required to redeem all of its outstanding shares of Series A preferred stock at $1 per share, plus all accrued and unpaid dividends declared. As of March 31, 2003, cumulative dividends totaled $187,661.

Common Stock

During the three months ended March 31, 2002, the Company issued 1,033,333 shares of common stock for cash totaling $90,000.

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NUTRASTAR INCORPORATED AND SUBSIDIARIES
NOTES TO CONDENSED, CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2003 (unaudited)

NOTE 10 - SHAREHOLDERS' DEFICIT (Continued)

Options
The expense, if any, of stock options issued to employees is recognized over the shorter of the term of service or vesting period. The expense of stock options issued to consultants or other third parties are recognized over the term of service. In the event services are terminated early, the entire amount is recognized. The unamortized portion of the expense to be recognized is recorded as deferred compensation.

NOTE 11 - LINES OF BUSINESS

For internal reporting purposes, management segregates the Company into two segments as follows for the three months ended March 31, 2003 and 2002:

	2003			
	NutraStar	NutraGlo	Eliminations	Total
Net sales	$ 13,304	$ 212,687	$ -	$ 225,
Income (loss) from operations	$ (416,017)	$ 52,002	$ -	$ (364,
Identifiable assets	$ 230,299	$ 619,912	$ (228,803)	$ 621,
Capital expenditures	$ -	$ -	$ -	$
Depreciation and amortization	$ 32,297	$ -	$ -	$ 32,

	2002			
	NutraStar	NutraGlo	Eliminations	Total
Net sales	$ 271,615	$ 22,742	$ -	$ 294,
Loss from operations	$ (1,007,415)	$ (62,168)	$ -	$ (1,069,
Identifiable assets	$ 659,393	$ 543,132	$ (182,137)	$ 1,020,
Capital expenditures	$ 41,124	$ -	$ -	$ 41,
Depreciation and				

amortization	$ 29,982	$ -	$ -	$ 29,

NOTE 12 - SUBSEQUENT EVENT

In April 2003, the Company sold 307,143 shares of common stock for cash totaling $21,500.

ITEM 2. MANAGEMENT'S DISCUSSION 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 the Company "expects," "anticipates" or "believes" are forward-looking statements. Investors should be aware that actual results may differ materially from the Company's 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.

Results of Operation

Three Month Period Ended March 31, 2003 versus 2002

During the quarter ended March 31, 2003, NutraStar generated net sales of $225,991 compared to $294,357 for the same quarter of 2002, a decrease of 23% in comparison to the first quarter of last year. The decrease was caused by several factors including certain key customers deferring purchases to a later date, a loss of certain customers choosing to obtain their stabilized rice brand from the RiceX Company ("RiceX") and an overall lack of working capital which prevented the Company from aggressively pursuing its marketing plan. Since July 2002 the Company's primary supplier, RiceX, has required cash on delivery for products sold to the Company.

The cost of goods sold for the quarter ended March 31, 2003 decreased 30% to $127,399 to $182,472 for the quarter ended March 31, 2002. This decrease reflects the reduced production of products for resale during the first quarter of 2003 due to the lack of adequate rice soluble inventory caused by the COD nature of purchases from RiceX. The Company's gross profit decreased to $98,592 for the quarter ended March 31, 2003 compared to $111,885 for the quarter ended March 31, 2002; while the gross profit margin increased from 38% in the first quarter of 2002 to 43.6% in the same period of 2003. This increase reflects the Company's focus on selling its own higher margin products as compared to the cross-selling of RiceX products.

Operating expenses declined 61% to $462,607 in the first quarter of 2003 compared to the same quarter in fiscal year 2002 which had operating expenses of $1,181,468. This decrease reflects the Company's decrease in employee related expenses of $55,000 compared to the same quarter of 2002 and a decrease of approximately $700,000 in cash and non-cash payments of professional and

consulting fees and non-cash employee compensation. The higher professional and consulting fees in the first quarter of 2002 relate to the Company's exchange reorganization and associated expenses.

The Company incurred an operating loss of $364,015 during the quarter ended March 31, 2003 compared to an operating loss of $1,069,583 during the quarter ended March 31, 2002. This 66% decrease in operating loss reflects the significant decrease in operating expenses relating to the Company's reduced business operations, coupled with the Company's cost cutting initiatives during the most recent quarter.

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During the quarter ended March 31, 2003, the Company recognized a sharp increase in interest expense to $17,191, which reflects interest paid on short-term promissory notes and other debt instruments outstanding during the quarter compared to only $740 for the quarter ended March 31, 2002. This expense resulted in the Company's overall net loss for the first quarter of 2003 to $381,206 compared to a net loss of $1,069,723 recorded for the comparable quarter of 2002. NutraStar also recognized accrued cumulative preferred dividends of $37,532 which increased the net loss attributable to common shareholders to $418,738 for the quarter ended March 31, 2003.

During the three months ended March 31, 2003, the Company sold approximately 90% of its net sales to one customer. During the same period of 2002, this customer represented approximately 52% of net sales.

Liquidity and Sources of Capital

NutraStar has incurred significant operating losses since its inception, and, as of March 31, 2003 NutraStar has an accumulated deficit of $8,697,579. At March 31, 2003, NutraStar had cash and cash equivalents of $37,982 and a net working capital deficit of $1,621,490.

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. During the quarter ended March 31, 2003, NutraStar raised a total of $240,422 from promissory notes. The interest rate on these promissory notes ranged from 8% to 24% per annum with two of the notes also being collateralized by a total of 450,000 shares of the Company's common stock. The Company also raised $90,000 from the sale of 1,033,333 shares of its common stock. During the quarter, NutraStar also agreed to collateralize a previous loan of $50,000 (plus $13,412 of accrued interest) with 634,121 shares of the Company's Series A preferred stock. For the three months ended March 31, 2003, NutraStar also changed the due dates on $180,800 of promissory notes from a specified due date to due-on-demand. This change was deemed necessary to avoid a default on some maturing notes. All of the loans made to the Company came from proceeds of notes payable to the Chairperson of NutraStar or other related parties. The Company has also conserved cash by deferring approximately $113,000 of compensation expenses. The Company will continue to pursue cost cutting or expense deferral strategies in order to conserve working capital. These strategies will limit the Company's implementation of its business plan and increase the future liabilities of the Company.

The Company is dependent on the proceeds from future debt or equity investments to fund 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 will 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.

On March 5, 2003, the Company entered into a consulting agreement with Recap Marketing for the purpose of assisting the Company in identifying and negotiating additional sources of capital to fund the Company's operations. The consultants will receive compensation of 7.5% of any cash proceeds received and an additional 2.5% of any proceeds received in the form of common stock of the Company. In addition, the consultants will receive one warrant for each dollar raised. The warrants are exercisable at $0.50 per share with a term of three years.

Due to the Company's need for outside capital and its operating losses, the financial statements include a going concern footnote explaining the uncertainties relating to the Company's ability to continue operations.

Contract With Key Supplier

NutraStar had entered into an agreement with The RiceX Company ("RiceX"), whereby RiceX would sell NutraStar its rice bran solubles and rice bran fiber complex at prices equal to the lower of RiceX's standard price or the price negotiated by other customers for like quantities and products (the "RiceX Agreement"). The RiceX Agreement also provided that RiceX would not sell any rice bran solubles or rice bran fiber concentrate products in the United States except to NutraStar. On July 9, 2002, this Agreement was terminated. As a result of this termination, NutraStar no longer has the right to be the exclusive distributor of the RiceX rice solubles and rice bran fiber concentrates in the United States; however, NutraStar has continued to buy such products from RiceX on a nonexclusive basis.

The RiceX Agreement also provided for a license from RiceX to NutraStar for the domestic use of four patents relating to the use of rice bran supplements to help treat diabetes and hyperlipidemia. Due to the fact that Ms. McPeak is a co-inventor of these patents and NutraStar has been primarily responsible for prosecuting such patents during the past two years, NutraStar has raised the issue of possible ownership rights in such patents. Although discussions have been held with RiceX regarding NutraStar's possible competing ownership rights, no resolution or formal action has yet occurred. NutraStar will continue to be allowed to utilize these patents until a new use arrangement can be negotiated.

In addition to the risks associated with the termination of the RiceX Agreement, the potential inability of RiceX to deliver the amount of product that NutraStar requires or the possible interruption in product delivery for any reason, would all have a material adverse effect on NutraStar's business, results from operations, and financial condition, because NutraStar could not readily find and implement alternative suppliers and likely not on advantageous terms. 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 may not be sufficient to meet NutraStar's long-term sales goals. NutraStar and RiceX are exploring ways to add production capacity during the next year.

Critical Accounting Policies

NutraStar's discussion and analysis of its financial conditions and results of operations are based upon its consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of financial statements require managers to make estimates and disclosures on the date of the financial statements. On an on-going basis, NutraStar evaluates its estimates, including, but not limited to, those related to revenue recognition. The Company uses authoritative pronouncements, historical experience and other assumptions as the basis for making judgments. Actual results could differ from those estimates. NutraStar believes that the following critical accounting policies affect its more significant judgments and estimates in the preparation of its consolidated financial statements.

Revenue recognition

NutraStar is required to make judgments based on historical experience and future expectations, as to the reliability of shipments made to its 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. NutraStar makes 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 the Company'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 NutraStar considers 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 its use of the acquired assets or the strategy of its overall business, and

(c) significant negative industry or economic trends.

When the Company determines 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, it measures any impairment based on a projected discounted cash flow method using a discount rate determined by its management to be commensurate with the risk inherent in its current business model.

Recently Issued Accounting Pronouncements

In June 2002, the FASB issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities." This statement addresses financial accounting and reporting for costs associated with exit or disposal activities and nullifies Emerging Issues Task Force ("EITF") Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)." This statement requires that a liability for a cost associated with an exit or disposal activity be recognized when the liability is incurred. Under EITF Issue 94-3, a liability for an exit cost, as defined, was recognized at the date of an entity's commitment to an exit plan. The provisions of this statement are effective for exit or disposal activities that are initiated after December 31, 2002 with earlier application encouraged. This statement is not applicable to the Company.

In October 2002, the FASB issued SFAS No. 147, "Acquisitions of Certain Financial Institutions." SFAS No. 147 removes the requirement in SFAS No. 72 and Interpretation 9 thereto, to recognize and amortize any excess of the fair value of liabilities assumed over the fair value of tangible and identifiable intangible assets acquired as an unidentifiable intangible asset. This statement requires that those transactions be accounted for in accordance with SFAS No. 141, "Business Combinations," and SFAS No. 142, "Goodwill and Other Intangible Assets." In addition, this statement amends SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," to include certain financial institution-related intangible assets. This statement is not applicable to the Company.

In December 2002, the FASB issued SFAS No. 148, "Accounting for Stock-Based Compensation - Transition and Disclosure," an amendment of SFAS No. 123. SFAS No. 148 provides alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. In addition, SFAS No. 148 amends the disclosure requirements of SFAS No. 123 to require more prominent and more frequent disclosures in financial statements about the effects of stock-based compensation. This statement is effective for financial statements for fiscal years ending after December 15, 2002. SFAS No. 148 will not have any impact on the Company's financial statements as management does not have any intention to change to the fair value method.

ITEM 3. CONTROLS AND PROCEDURES

Within 90 days prior to the date of this Form 10-QSB, the Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer along with the Company's Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures pursuant to Exchange Act Rule 13a-14. Based upon that evaluation, the Company's Chief Executive Officer along with the Company's Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective in timely

recording, processing summarizing and reporting material information relating to the Company required to be disclosed in this Form 10-QSB.

There have been no significant changes in the Company's internal controls or in other factors, which could significantly affect internal controls subsequent to the date the Company carried out its evaluation.

PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

From time to time the Company is subject to legal proceedings and claims in the ordinary course of business including claims by certain of its vendors.

Information regarding current litigation is set forth in Note 9 of the Notes to Condensed, Consolidated Financial Statements included in Part I, Item 1 of this report.

ITEM 2. CHANGES IN SECURITIES

During the quarter, NutraStar agreed to collateralize a previously unsecured loan of $50,000 (plus $13,412 of accrued interest) with 634,121 shares of the Company's Series A Preferred Stock. During the quarter NutraStar also changed the due dates on $180,800 of promissory notes from a specified due date to due-on-demand.

Sales of Unregistered Securities During the Quarter

On January 30, 2003, the Company entered into a promissory note agreement for $20,422 with the Chief Executive Officer of the Company. The note bears interest at 10% per annum and is due on demand.

On February 7, 2003, the Company entered into a promissory note agreement for $90,000 with the Chief Executive Officer of the Company. The note bears interest at 8% per annum, is collateralized by all of the assets of the Company, and is due on May 6, 2003.

On February 18, 2003, the Company entered into a promissory note agreement for $60,000 with the Chief Executive Officer of the Company. The note bears interest at 10% per annum and is due on March 18, 2003.

On March 5, 2003, the Company entered into a promissory note agreement for $40,000 with a related party. The note bears interest at 2% per month, is collateralized by 400,000 shares of the Company 's common stock, and is due on June 3, 2003.

On March 10, 2003, the Company entered into a promissory note agreement for $5,000 with a related party. The note bears interest at 2% per month, is collateralized by 50,000 shares of the Company 's common stock, and is due on June 8, 2003.

On March 31, 2003, the Company sold 1,033,333 shares of its common stock to two individuals for total proceeds of $90,000.

All of the above issuances of promissory notes or stock were made without any

public solicitation, to a limited number of accredited investors or related individuals or entities and were acquired for investment purposes only. Each of the individuals or entities had access to information about the Company and were

deemed capable of protecting their own interests. The notes and stock were issued pursuant to the private placement exemption provided by Section 4(2) of the Securities Act of 1933. These are deemed to be "restricted securities" as defined in Rule 144 under the 1933 Act and the notes evidencing the loans and the stock certificates bear a legend stating the restrictions on resale.

ITEM 5. OTHER INFORMATION

Subsequent to Mr. Ferrara's resignation, in November 2002, an "Office of the President" was created which included Patricia McPeak (the CEO) and two outside consultants, Etienne Taylor and Brian Jones. Messrs. Taylor and Jones specialize in managing corporate restructuring. The Office of the President was responsible for the management of the day-to-day operations of NutraStar. The Office of the President was disbanded on January 31, 2003 and Messrs. Taylor and Jones were terminated as consultants to NutraStar. As of January 31, 2003, Ms. McPeak assumed the duties of President of NutraStar.

Due to financial constraints, Danny Lowell, the Company's Chief Information Officer, was laid-off effective February 18, 2003.

Subsequent to the end of the quarter reported herein, the Company hired John Howell as its new President and Chief Operating Officer. Mr. Howell brings extensive experience in corporate restructuring most recently having worked with Kingdom Ventures, Inc. in Nevada. These positions were assumed from Patricia McPeak who remains Chairperson of the Board of Directors and Chief Executive Officer.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits:

(i) 99.1 - Certification by CEO and CFO pursuant to Sections 906 of the Sarbanes-Oxley Act of 2002.

(b) Reports on Form 8-K: None

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: May 19, 2003 s/s James Kluber

James Kluber, Authorized Officer and
Chief Financial Officer
(Principal Accounting Officer)

CERTIFICATION FOR QUARTERLY REPORTS ON FORM 10-QSB

I, Patricia M. Peak, certify that:

1. I have reviewed this quarterly report on Form 10-QSB of NutraStar Incorporated ("Registrant");

2 Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the Registrant as of, and for, the periods presented in this quarterly report;

4. The Registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the Registrant and we have:

a) designed such disclosure controls and procedures to ensure that material information relating to the Registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

b) evaluated the effectiveness of the Registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and

c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The Registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the Registrant's auditors and the audit committee of Registrant's board of directors (or persons performing the equivalent function):

a) all significant deficiencies in the design or operation of internal controls which could adversely affect the Registrant's ability to record, process, summarize and report financial data and have identified for the Registrant's auditors any material weaknesses in internal controls; and

b) any fraud, whether or not material, that involves management or other employees who have a significant role in the Registrant's internal controls; and

6. The Registrant's other certifying officer and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: May 19, 2003

/s/ Patricia McPeak

Patricia McPeak, Chief Executive Officer

CERTIFICATION FOR QUARTERLY REPORTS ON FORM 10-QSB

I, James Kluber, certify that:

1. I have reviewed this quarterly report on Form 10-QSB of NutraStar Incorporated ("Registrant");

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the Registrant as of, and for, the periods presented in this quarterly report;

4. The Registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the Registrant and we have:

a) designed such disclosure controls and procedures to ensure that material information relating to the Registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

b) evaluated the effectiveness of the Registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and

c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The Registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the Registrant's auditors and the audit committee of Registrant's board of directors (or persons performing the equivalent function):

a) all significant deficiencies in the design or operation of internal

controls which could adversely affect the Registrant's ability to record, process, summarize and report financial data and have identified for the Registrant's auditors any material weaknesses in internal controls; and

b) any fraud, whether or not material, that involves management or other employees who have a significant role in the Registrant's internal controls; and

6. The Registrant's other certifying officer and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: May 19, 2003

/s/ James Kluber

James Kluber, Chief Financial Officer