

MEDSTONE INTERNATIONAL INC/
Form 10-Q
May 14, 2003

Table of Contents

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended **March 31, 2003**

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission file number 0-16752

MEDSTONE INTERNATIONAL, INC.

(Exact name of registrant as specified in its charter)

DELAWARE

66-0439440

(State or other jurisdiction of incorporation or organization)

(I.R.S. Employer Identification No.)

100 Columbia, Suite 100, Aliso Viejo, California

92656

(Address of principal executive offices)

(Zip code)

Registrant's telephone number, including area code: **(949) 448-7700**

Not Applicable

(Former name, former address and former fiscal year, if changed, since last report)

Indicate by check mark whether the registrant (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 registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.

Yes No

The number of shares of the Common Stock of the registrant outstanding as of May 1, 2003 was 3,758,220

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act).

Yes No

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The number of shares of the Common Stock of the registrant outstanding as of June 30, 2002 was 3,920,020. The number of shares voting and non-voting Common Stock held by non-affiliates on such date was 3,827,312 with an approximate aggregate market value of \$19,327,926.

Table of Contents

MEDSTONE INTERNATIONAL, INC.

INDEX TO FORM 10-Q

| | Page No. |
|---|---|
| | <hr/> |
| <u>PART I. FINANCIAL INFORMATION</u> | |
| Item 1. | Financial Statements: |
| | <u>Consolidated Balance Sheets March 31, 2003 (Unaudited) and December 31, 2002</u> 3 |
| | <u>Consolidated Statements of Income Three Months Ended March 31, 2003 and 2002 (Unaudited)</u> 4 |
| | <u>Consolidated Statement of Stockholders' Equity Three Months Ended March 31, 2003 (Unaudited)</u> 5 |
| | <u>Consolidated Statements of Cash Flows Three Months Ended March 31, 2003 and 2002 (Unaudited)</u> 6 |
| | <u>Notes to Unaudited Consolidated Financial Statements</u> 7 |
| Item 2. | <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u> 11 |
| Item 3. | <u>Market Risk Changes</u> |
| Item 4. | <u>Controls and Procedures</u> |
| <u>PART II. OTHER INFORMATION</u> | |
| Item 1. | <u>Legal Proceedings</u> 15 |
| Item 2. | <u>Changes in Securities</u> 15 |
| Item 3. | <u>Defaults Upon Senior Securities</u> 15 |
| Item 4. | <u>Submission of Matters to a Vote of Security Holders</u> 15 |
| Item 5. | <u>Other Information</u> 15 |
| Item 6. | <u>Exhibits and Reports on Form 8-K</u> 15 |
| | <u>Signatures</u> 16 |
| | <u>Certifications</u> |

Table of Contents**MEDSTONE INTERNATIONAL, INC.
CONSOLIDATED BALANCE SHEETS**

| | <u>March 31, 2003</u> | <u>December 31, 2002</u> |
|--|---------------------------|------------------------------|
| | | (Unaudited) |
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 1,940,332 | \$ 2,050,466 |
| Short-term investments held to maturity | 4,341,831 | 4,323,491 |
| Accounts receivable, less allowance for doubtful accounts of \$931,769 and \$871,769 at March 31, 2003 and December 31, 2002, respectively | 3,289,013 | 3,720,410 |
| Income taxes receivable | 589,375 | 589,375 |
| Inventories, less allowance for inventory obsolescence of \$716,700 and \$642,712 at March 31, 2003 and December 31, 2002, respectively | 6,405,923 | 6,440,304 |
| Deferred tax assets | 955,877 | 955,877 |
| Prepaid expenses and other current assets | 1,007,585 | 647,169 |
| | <u>18,529,936</u> | <u>18,727,092</u> |
| Buildings, property and equipment, at cost: | | |
| Building | 359,324 | 359,324 |
| Lithotripters | 13,750,702 | 13,524,440 |
| Equipment, furniture and fixtures | 3,387,807 | 3,368,431 |
| Leasehold improvements | 177,318 | 177,318 |
| | <u>17,675,151</u> | <u>17,429,513</u> |
| Less accumulated depreciation and amortization | (13,989,559) | (13,602,049) |
| | <u>3,685,592</u> | <u>3,827,464</u> |
| Net property and equipment | 3,685,592 | 3,827,464 |
| Goodwill, net | 2,929,897 | 2,929,897 |
| Investment in unconsolidated subsidiaries | 794,744 | 734,083 |
| Net investment in sale-type lease | 119,514 | 169,428 |
| Other assets, net | 86,964 | 93,243 |
| | <u>\$ 26,146,647</u> | <u>\$ 26,481,207</u> |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Accounts payable | \$ 715,166 | \$ 900,295 |
| Accrued expenses | 311,168 | 267,229 |
| Accrued payroll expenses | 344,302 | 366,855 |
| Customer deposits | 120,187 | 75,175 |
| Deferred revenue | 469,581 | 494,704 |
| | <u>1,960,404</u> | <u>2,104,258</u> |
| Total current liabilities | 1,960,404 | 2,104,258 |
| Deferred tax liabilities | 639,224 | 639,224 |
| Minority interest | 395,606 | 423,224 |
| Deferred rent | 79,135 | 82,613 |
| Commitments and contingencies (Notes 7 and 8) | | |
| Stockholders' equity: | | |
| Common stock - \$.004 par value, 20,000,000 shares authorized, 5,742,670 shares issued at both March 31, 2003 and December 31, 2002 | 22,971 | 22,971 |

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| | | |
|---|----------------------|----------------------|
| Additional paid-in capital | 19,646,388 | 19,646,388 |
| Accumulated earnings | 16,228,627 | 16,350,292 |
| Accumulated other comprehensive loss | (59,999) | (22,054) |
| Treasury stock, at cost, 1,984,450 at both March 31, 2003 and December 31, 2002, respectively | (12,765,709) | (12,765,709) |
| Total stockholders equity | 23,072,278 | 23,231,888 |
| | <u>\$ 26,146,647</u> | <u>\$ 26,481,207</u> |

See accompanying notes

- 3 -

Table of Contents

MEDSTONE INTERNATIONAL, INC.
CONSOLIDATED STATEMENTS OF INCOME
Three months ended March 31, 2003 and 2002
(Unaudited)

| | 2003 | 2002 |
|---|---------------------|-------------------|
| Revenues: | | |
| Procedures, maintenance fees and fee-for-service | \$ 4,068,423 | \$ 4,337,435 |
| Net equipment sales | 719,127 | 1,896,443 |
| Interest income | 40,501 | 82,123 |
| Total revenues | 4,828,051 | 6,316,001 |
| Costs and operating expenses: | | |
| Cost of procedures and maintenance fees | 2,231,259 | 2,426,949 |
| Cost of equipment sales | 795,404 | 1,474,909 |
| Research and development | 409,061 | 260,939 |
| Selling | 617,033 | 812,215 |
| General and administrative | 802,119 | 817,490 |
| Total costs and operating expenses | 4,854,876 | 5,792,502 |
| Operating income (loss) | (26,825) | 523,499 |
| Other expense (income) | 23,820 | (1,887) |
| Minority interests: | | |
| Minority interest in subsidiaries income | 170,381 | 170,019 |
| Equity in loss (income) from unconsolidated subsidiary | (69,161) | 30,359 |
| Total minority interest | 101,220 | 200,378 |
| Income (loss) before provision for income taxes | (151,865) | 325,008 |
| Provision for (benefit from) income taxes | (30,200) | 157,800 |
| Net income (loss) | \$ (121,665) | \$ 167,208 |
| Net income (loss) per share: | | |
| Basic | \$ (.03) | \$.04 |
| Diluted | N/A | \$.04 |
| Number of shares used in the computation of earnings (loss) per share: | | |
| Basic | 3,758,220 | 3,954,553 |
| Diluted | N/A | 3,954,553 |

See accompanying notes.

Table of Contents

MEDSTONE INTERNATIONAL, INC.
CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY

| | Common Stock | | Additional paid-in capital | Accumulated earnings | Accumulated Other Comprehensive loss | Treasury Stock | Total |
|--|---------------------|------------------|----------------------------------|-------------------------|---|------------------------|----------------------|
| | Number of shares | Amount | | | | | |
| Balance at December 31, 2002 | 3,758,220 | \$ 22,971 | \$ 19,646,388 | \$ 16,350,292 | \$ (22,054) | \$ (12,765,709) | \$ 23,231,888 |
| Net loss | | | | (121,665) | | | (121,665) |
| Other comprehensive income: | | | | | | | |
| Unrealized loss on foreign currency translation, net | | | | | (37,945) | | (37,945) |
| Total comprehensive loss | | | | | | | (159,610) |
| Balance at March 31, 2003(Unaudited) | 3,758,220 | \$ 22,971 | \$ 19,646,388 | \$ 16,228,627 | \$ (59,999) | \$ (12,765,709) | \$ 23,072,278 |

See accompanying notes.

Table of Contents**MEDSTONE INTERNATIONAL, INC.****CONSOLIDATED STATEMENTS OF CASH FLOWS**

Three months ended March 31, 2003 and 2002
(Unaudited)

| | <u>2003</u> | <u>2002</u> |
|---|---------------------|---------------------|
| Cash flows from operating activities: | | |
| Net income (loss) | \$ (121,665) | \$ 167,208 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 412,817 | 433,876 |
| Provision for doubtful accounts | 60,000 | 60,000 |
| Provision for inventory obsolescence | 75,000 | 42,000 |
| Minority interest in partnerships | 170,382 | 170,019 |
| Minority loss (equity) in unconsolidated subsidiary | (60,661) | 30,359 |
| Changes in assets and liabilities: | | |
| Accounts receivable | 141,784 | 122,995 |
| Inventories | (40,619) | 667,608 |
| Prepaid expenses and other current assets | (80,889) | (37,721) |
| Accounts payable and accrued expenses | (141,190) | (159,622) |
| Accrued payroll expenses | (22,553) | (24,571) |
| Accrued income taxes | | |
| Deferred revenue | (25,123) | 111,109 |
| Customer deposits | 45,012 | (336,948) |
| Other, net | (35,011) | (29,721) |
| Net cash provided by operating activities | <u>377,284</u> | <u>1,216,591</u> |
| Cash flows from investing activities: | | |
| Purchase of short-term investments | (1,177,257) | (1,169,251) |
| Proceeds from sales of short-term investments | 1,158,917 | 1,139,288 |
| Investment in sales type lease | | (7,860) |
| Distribution of minority interest | (198,000) | (188,000) |
| Purchase of property and equipment, net | (267,600) | (635,514) |
| Net cash used in by investing activities | <u>(483,940)</u> | <u>(861,337)</u> |
| Cash flows from financing activities: | | |
| Purchase of treasury stock | | (819,750) |
| Deferral of rent payments | (3,478) | 850 |
| Net cash used in financing activities | <u>(3,478)</u> | <u>(818,900)</u> |
| Net change in cash and cash equivalents | (110,134) | (463,646) |
| Cash and equivalents at beginning of period | 2,050,466 | 1,928,731 |
| Cash and equivalents at end of period | <u>\$ 1,940,332</u> | <u>\$ 1,465,085</u> |
| Supplemental cash flow disclosures: | | |
| Cash paid during the period for: | | |
| Income taxes | \$ 15,145 | \$ 6,288 |

See accompanying notes.

- 6 -

Table of Contents**MEDSTONE INTERNATIONAL, INC.****NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2003****A. Basis of presentation**

The accompanying condensed consolidated financial statements include the accounts of Medstone International, Inc. and its subsidiaries (the Company). All significant intercompany transactions and accounts have been eliminated.

In the opinion of the Company's management, the accompanying unaudited condensed consolidated financial statements include all adjustments (which consist only of normal recurring adjustments) necessary for a fair presentation of its consolidated financial position at March 31, 2003 and consolidated results of operations and cash flows for the periods presented. Although the Company believes that the disclosures in these financial statements are adequate to make the information presented not misleading, certain information and disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted. These financial statements should be read in conjunction with the Company's audited financial statements included in the Company's 2002 Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 31, 2003. Results of operations for the three months ended March 31, 2003 are not necessarily indicative of results to be expected for the full year.

The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America requires management to make assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from these estimates.

B. Accumulated Other Comprehensive Loss:

The components of accumulated other comprehensive (loss)/income are as follows:

| | Currency Translation Adjustment |
|--|--|
| Balance at December 31, 2002 | \$ (22,054) |
| Foreign currency translation adjustments | (37,945) |
| Balance at March 31, 2003 | \$ (59,999) |

The functional currency of the investment in foreign subsidiary is considered to be the United States dollar.

Table of Contents

The earnings associated with the Company's investment in its foreign subsidiary are considered to be permanently invested and no provision for U.S. federal and state income taxes on those earnings or translation adjustments has been provided.

For the three months ended March 31, 2003, total comprehensive loss was \$159,610. For the three months ended March 31, 2002, total comprehensive income was \$137,491.

C. Business Segments

The Company operates in two business segments, equipment sales and fees for procedures, maintenance and management.

| | Three Months Ended | |
|---|---------------------------|-----------------------|
| | March 31, 2003 | March 31, 2002 |
| | (Unaudited) | (Unaudited) |
| Revenue: | | |
| Equipment sales | \$ 719,127 | \$ 1,896,443 |
| Fees for procedures, maintenance fees and fee-for-service | 4,068,423 | 4,337,435 |
| | <u>\$ 4,787,550</u> | <u>\$ 6,233,878</u> |
| Operating income (loss): | | |
| Equipment sales | \$ (374,967) | \$ (139,942) |
| Fees for procedures, maintenance fees and fee-for-service | 348,145 | 663,441 |
| | <u>\$ (26,822)</u> | <u>\$ 523,499</u> |

D. Per share information

Basic net income per share is computed by dividing income available to common stockholders by the weighted average number of common shares outstanding. Diluted net income per share includes the effect of the potential shares outstanding, including dilutive stock options and warrants using the treasury stock method.

Common equivalent shares result from the assumed exercise of outstanding dilutive securities when applying the treasury stock method. Fully diluted per share information is not presented for periods in which the effect is antidilutive.

Table of Contents

The following table sets forth the computation of earnings per share:

| | Three Months Ended | |
|---|--------------------|-------------------|
| | March 31, 2003 | March 31, 2002 |
| | (Unaudited) | (Unaudited) |
| Numerator: Net income (loss) | \$ (121,665) | \$ 167,208 |
| Denominator for weighted average shares outstanding | 3,758,220 | 3,954,553 |
| Basic income (loss) per share | \$ (.03) | \$.04 |
| Effect of dilutive securities: | | |
| Weighted average shares outstanding | N/A | 3,954,553 |
| Stock options | N/A | |
| Denominator for diluted earnings per share | N/A | 3,954,553 |
| Diluted earnings per share | N/A | \$.04 |

E. Inventories

Effective January 1, 2003, the Company changed its method of accounting for inventories from first-in first-out to an average cost method. The impact of this change was not material to the financial statements.

Inventories are stated at the lower of average cost or market and consist of the following:

| | March 31, 2003 | December 31, 2002 |
|--------------------------|-------------------|----------------------|
| Raw materials | \$ 5,411,755 | \$ 5,231,574 |
| Work in process | 306,134 | 312,665 |
| Finished goods | 1,404,734 | 1,538,777 |
| Gross inventories | 7,122,623 | 7,083,016 |
| Less: Inventory reserves | (716,700) | (642,712) |
| Net inventories | \$ 6,405,923 | \$ 6,440,304 |

Table of Contents

F. Contingencies

From time to time, the Company is subject to legal actions and claims for personal injuries or property damage related to patients who use its products. The Company has obtained a liability insurance policy providing coverage for product liability and other claims. Management does not believe that the resolution of any current proceedings will have a material financial impact on the Company or the consolidated financial statements.

- 10 -

Table of Contents

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

The following discussion and analysis should be read in conjunction with the Company's audited financial statements and Management's Discussion and Analysis of Financial Condition and Results of Operations included in the Company's 2002 Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 31, 2003.

In the ordinary course of business, the company has made a number of estimates and assumptions relating to the reporting of results of operations and financial condition in the preparation of its financial statements in conformity with accounting principles generally accepted in the United States of America. Actual results could differ significantly from those estimates under different assumptions and conditions. The Company believes that the following discussion addresses the Company's most critical accounting policies, which are those that are most important to the portrayal of the Company's financial condition and results. The Company constantly re-evaluates these significant factors and makes adjustments where facts and circumstances dictate. Historically, actual results have not significantly deviated from those determined using the necessary estimates inherent in the preparation of financial statements. Estimates and assumptions include, but are not limited to, customer receivables, inventories, equity investments, fixed asset lives, contingencies and litigation. The Company has also chosen certain accounting policies when options were available, including:

The average cost method to value a majority of our inventories; and
The intrinsic value method, or APB Opinion No. 25, to account for our common stock incentive awards; and
We record an allowance for credit losses based on estimates of customers' ability to pay. If the financial condition of our customers were to deteriorate, additional allowances may be required.

These accounting policies are applied consistently for all periods presented. Our operating results would be affected if other alternatives were used. Information about the impact on our operating results is included in the footnotes to our consolidated financial statements.

Results of Consolidated Operations

General

Medstone manufactures, markets and maintains lithotripters, and utilizes its Fee-for-Service Program to supply lithotripsy equipment to providers on a per procedure basis. The lithotripters manufactured by Medstone is approved to treat both kidney stones and gallstones. The Company is also marketing a urology imaging and treatment table, used for various urological functions, mobile urology and pain management table to serve the mobile treatment market and various radiology

Table of Contents

room equipment, capitalizing on the relationships that the Company has with radiology equipment manufacturers. To date, the Company's consolidated revenues have come primarily from Medstone's lithotripsy business.

As a manufacturer of medical devices, the Company is vertically integrated by offering its medical devices directly to providers. It currently offers lithotripsy procedures using 14 mobile systems, one fixed site and 23 transmobile lithotripters located throughout the United States on a per procedure basis. With the ability to offer state-of-the-art equipment at reasonable prices, Medstone continues to consider this part of its business as an integral part of its business plan.

Three Months Ended March 31, 2003 Compared to Three Months Ended March 31, 2002

The Company recognized total revenue of \$4.8 million in the first quarter of 2003 compared to \$6.3 million in the first quarter of 2002, or a decrease of 24%. Revenues from procedures, maintenance and management fees decreased from \$4.3 million in the three months ended March 31, 2002 to \$4.1 million in the three months ended March 31, 2003 due to continuing decline in the average per patient charges on the Company's fee-for-service equipment on essentially the same patient count along with a decrease in the third party patient count and corresponding per patient charge in the current year. Also decreasing were the spares revenues as a lower number of shipments occurred in the current year compared to the same period of the prior year. Equipment revenues also decreased to \$0.7 million in the quarter ending March 31, 2003 from \$1.9 million in the comparable quarter of the prior year, or a 62% decrease. The Company did not ship any lithotripsy systems in the quarter ending March 31, 2003 compared to three systems in the same period in the prior year. The Company also realized revenue on shipment of one UroPro urology systems in the current year compared to three systems in the three months ended March 31, 2002. Shipments of major medical devices decreased dramatically due to the uncertainty in the government sector regarding funding of medical devices and the private healthcare sector's emphasis on cost containment. The number of patient handling tables shipped in the three months ended March 31, 2003 increased to 31 units compared to 16 units in the same period of 2002, but average selling price decreased slightly in the current year when compared to the prior year.

Interest income decreased by 51% in the first quarter of 2003 when compared to the same period of the prior year due to a significant decline in investment yields and a decrease in the average invested balance.

Recurring revenue cost of sales decreased to 55% of sales in the quarter ended March 31, 2003 compared to 56% in the same quarter of the prior year. This decrease is due to lower depreciation for mobile equipment and lower equipment rental expenses on vans and trucks as service areas decrease in size and fixed site fee-for-service units are utilized. Cost of sales on equipment sales increased to 111% of sales in the three months ended March 31, 2003 compared to 78% of sales in the same period of 2002. This increase is due to very low equipment sales activity

Table of Contents

and fixed costs of production. Overall cost of sales, as a percentage of revenue (excluding interest), remained constant at 63% in the first quarter of 2003 compared to 63% in the first quarter of 2002.

Research and development costs increased by 57%, or \$148,000, in the first quarter of 2003 when compared to the first quarter of 2002 due to increased spending for the UroPro Vista model being developed for shipment in the 4th quarter of 2003 and the MultiRad imaging system, with shipment expected by the 3rd quarter of 2003.

Selling costs decreased to \$617,000 in the first quarter of 2003 compared to \$812,000 in the same period of the prior year, a change of \$195,000 or 24% due to 2002's higher commission expenses from higher equipment sales and the advertising and consulting costs incurred for recruitment of patients for the gallstone study.

Total minority interest expense decreased to \$101,000 in the three months ended March 31, 2003 compared to \$200,000 in the same period of the prior year due to recognition of operating profits at Arcoma AB in the current year compared to operating losses in Arcoma AB operations in 2002. The Company's expense for minority distributions in the Northern Nevada and Southern Idaho operations remained constant in both periods.

Liquidity and Capital Resources

At March 31, 2003, the Company had cash and short-term investments of approximately \$6.3 million. These funds were generated from continuing operating activities.

As of March 31, 2003, the Company held 13,571 shares of CorAutus Genetics, Inc. common stock, with an approximate market value of \$18,864. The Company will continue to liquidate its holdings in this Company as markets allow.

The Company's long-term capital expenditure requirements will depend on numerous factors, including the progress of the Company's research and development programs, the time required to obtain regulatory approvals, the resources that the Company devotes to the development of self-funded products, proprietary manufacturing methods and advanced technologies, the costs of acquisitions and/or new revenue opportunities, the ability of the Company to obtain additional licensing arrangements and to manufacture products under those arrangements, and the demand for its products if and when approved and possible acquisitions of products, technologies and companies.

The Company believes that its existing working capital and funds anticipated to be generated from operations will be sufficient to meet the cash needs for continuation of its present operations during 2003.

Table of Contents

Safe Harbor Statement Under the Private Securities Litigation Reform Act of 1995

Forward-looking statements in this report, including without limitation, statements relating to the Company's plans, strategies, objectives, expectations, intentions and adequacy of resources, are made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Investors are cautioned that such forward-looking statements involve risks and uncertainties including without limitation the following: (i) the Company's plans, strategies, objections, expectations and intentions are subject to change at any time at the discretion of the Company, (ii) the Company's plans and results of operations will be affected by the Company's ability to manage its growth; (iii) the Company's businesses are highly competitive and the entrance of new competitors into or the expansion of the operations by existing competitors in the Company's markets and other changes could adversely affect the Company's plans and results of operations; and (iv) other risks and uncertainties indicated from time to time in the Company's filings with the Securities and Exchange Commission.

Item 3. Market Risk Changes

The Company has no significant market risk changes for the period ended March 31, 2003.

Item 4. Controls and Procedures

Within the 90-day period prior to the date of this report, the Company carried out an evaluation, under the supervision and with the participation of the Company's management, including its Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures pursuant to Exchange Act Rule 15d-14 (c).] Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective in a timely manner to alert them to material information relating to the Company which is required to be included in the Company's periodic Securities and Exchange Commission filings. There have been no significant changes in the Company's internal controls or in other factors that could significantly affect these controls subsequent to the evaluation date.

Table of Contents

MEDSTONE INTERNATIONAL, INC.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

Previously reported.

Item 2. Changes in Securities

None

Item 3. Defaults upon Senior Securities

None

Item 4. Submission of Matters to a Vote of Security Holders

None

Item 5. Other Information

None

Item 6. Exhibits and Reports on Form 8-K

(a) The following exhibits are included herein:

- 99.1 Certification by Chairman and Chief Executive Officer
- 99.2 Certification by Chief Financial Officer

(b) Reports on Form 8-K.

None.

- 15 -

Table of Contents

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

MEDSTONE INTERNATIONAL, INC.
A Delaware corporation

Date: May 6, 2003

/s/ MARK SELAWSKI

Mark Selawski
Chief Financial Officer
(Principal financial and accounting officer)

- 16 -

Table of Contents

Medstone International, Inc.

CERTIFICATION

I, David V. Radlinski, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Medstone International, Inc., the 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 officers 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 officers 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 officers 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 6, 2003

/s/ DAVID V. RADLINSKI

David V. Radlinski
Chairman and Chief Executive Officer

Table of Contents

Medstone International, Inc.

CERTIFICATION

I, Mark Selawski, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Medstone International, Inc., the 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 officers 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 officers 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 officers and I have indicated in this annual 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 6, 2003

/s/ MARK SELAWSKI

Mark Selawski
Chief Financial Officer

Table of Contents

Exhibit Index

- 99.1 Certification by Chairman and Chief Executive Officer
- 99.2 Certification by Chief Financial Officer

- 19 -