VITAL SIGNS INC
Form 10-Q
May 15, 2002

SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549

FORM 10-Q

(Mark one)

[X] Quarterly report pursuant to Section 13 or 15 (d) of the Securities Exchange Act of 1934 for the quarterly period ended March 31, 2002 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: 0-18793

VITAL SIGNS, INC.
(Exact name of registrant as specified in its charter)

New Jersey	11-2279807
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

20 Campus Road
Totowa, New Jersey 07512
(Address of principal executive office, including zip code)

973-790-1330
(Registrant's telephone number, including area code)

(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 X No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

At May 10, 2002 there were 12,906,232 shares of Common Stock, no par value, outstanding.

VITAL SIGNS, INC.

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PART I.

Financial Information

Item 1.

Financial Statements

Certain information and footnote disclosures required under generally accepted accounting principles have been condensed or omitted from the following consolidated financial statements pursuant to the rules and regulations of the Securities and Exchange Commission. Vital Signs, Inc. (the "registrant" or the "Company" or "Vital Signs") believes that the disclosures are adequate to assure that the information presented is not misleading in any material respect. It is suggested that the following consolidated financial statements be read in conjunction with the year-end consolidated financial statements and notes thereto included in the registrant's Annual Report on Form 10-K for the year ended September 30, 2001.

The results of operations for the interim periods presented herein are not necessarily indicative of the results to be expected for the entire fiscal year.

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INDEPENDENT ACCOUNTANT'S REPORT

To the Board of Directors
Vital Signs, Inc.

We have reviewed the accompanying consolidated balance sheet of Vital Signs, Inc. as of March 31, 2002 and the related consolidated statements of income for the three-month and six-month periods ended March 31, 2002 and 2001, and cash flows for the six-month periods ended March 31, 2002 and 2001. These financial statements are the responsibility of the Company's management.

We conducted our reviews in accordance with standards established by the American Institute of Certified Public Accountants. A review of interim financial information consists principally of applying analytical procedures to financial data and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole.

Accordingly, we do not express such an opinion.

Based on our reviews, we are not aware of any material modifications that should be made to the accompanying consolidated financial statements for them to be in conformity with generally accepted accounting principles.

GOLDSTEIN GOLUB KESSLER LLP
New York, New York

May 8, 2002

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VITAL SIGNS, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

	March 31, 2002 (In (Unaudited)
ASSETS	
Current Assets:	
Cash and cash equivalents	$ 33,002
Accounts receivable, less allowance for doubtful accounts of $840 and $436 respectively	35,548
Inventory	24,812
Prepaid expenses and other current assets	8,669
Total Current Assets	102,031
Property, plant and equipment - net	36,576
Marketable securities	465
Goodwill	65,601
Deferred income taxes	2,817
Other assets	2,727
Total Assets	$210,217
LIABILITIES AND STOCKHOLDERS' EQUITY	
Current Liabilities:	
Accounts payable	$ 6,075
Current portion of long-term debt	394
Accrued expenses	7,813
Notes payable - bank	4,943

Other current liabilities	8,691
Total Current Liabilities	27,916
Long term debt	1,634
Total Liabilities	29,550
Commitments and contingencies	
Minority interest in subsidiary	3,019
Stockholders' Equity	
Common stock - no par value; authorized 40,000,000 shares, issued and outstanding 12,959,032 and 12,935,656 shares, respectively	31,500
Accumulated other comprehensive loss	(2,281)
Retained earnings	148,429
Stockholders' equity	177,648
Total Liabilities and Stockholders' Equity	$210,217

(See Notes to Consolidated Financial Statements)

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VITAL SIGNS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

	For the Six
	March
	2002
	(In Thousands Excep
Revenue:	
Net sales	$74,623
Service revenue	10,935
	85,558
Cost of goods sold and services performed:	
Cost of goods sold	37,035
Cost of services performed	6,499
	43,534
Gross profit	42,024

Operating expenses:	
Selling, general and administrative	21,766
Research and development	3,670
Total operating expenses	25,436
Operating Income	16,588
Other (income) expense:	
Interest income	(385)
Interest expense	59
Other expense (income)	142
Reversal of litigation accrual	(5,006)
Goodwill amortization	---
Total other (income) expense	(5,190)
Income before provision for income taxes and minority interest in income of consolidated subsidiary	21,778
Provision for income taxes	7,367
Income before minority interest in income of consolidated subsidiary	14,411
Minority interest in income of consolidated subsidiary	154
Net income	$14,257
Earnings per Common Share:	
Basic net income per share	$ 1.11
Diluted net income per share	$ 1.09
Basic weighted average number of shares	12,890
Diluted weighted average number of shares	13,036
Dividends paid per share	$ .08

(See Notes to Consolidated Financial Statements)

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VITAL SIGNS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

For the Three
March

	2002
	(In Thousands Except
Revenue:	
Net sales	$37,697
Service revenue	5,762
	43,459
Cost of goods sold and services performed:	
Cost of goods sold	19,773
Cost of services performed	3,272
	23,045
Gross Profit	20,414
Operating expenses:	
Selling, general and administrative	11,354
Research and development	1,867
Total operating expenses	13,221
Operating income:	7,193
Other (income) expense:	
Interest income	(154)
Interest expense	---
Other expense (income)	74
Reversal of litigation accrual	(5,006)
Goodwill amortization	---
Total other (income) expense	(5,086)
Income before provision for income taxes and minority interest in income of consolidated subsidiary	12,279
Provision for income taxes	4,181
Income before minority interest in income of consolidated subsidiary	8,098
Minority interest in income of consolidated subsidiary	154
Net income	$ 7,944
Earnings per Common Share:	
Basic net income per share	$ 0.62
Diluted net income per share	$ 0.61
Basic weighted average number of shares	12,909
Diluted weighted average number of shares	13,060
Dividends paid per share	$ .04

(See Notes to Consolidated Financial Statements)

VITAL SIGNS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF CASH FLOWS
(Unaudited)

	For the Six Mon March 2002
Cash Flows from Operating Activities:	
Net income	$ 14,257
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:	
Depreciation and amortization	2,195
Foreign currency gain	--
Amortization of goodwill	--
Deferred taxes	1,914
Non cash gain on litigation accrual reversal	(5,006)
Minority interest in income of consolidated subsidiary	154
Changes in operating assets and liabilities:	
Decrease (increase) in accounts receivable	39
Decrease (increase) in inventory	1,421
Decrease in prepaid expenses and other current assets	2,548
Decrease in other current liabilities	(495)
Decrease in other assets	342
Increase in accounts payable and accrued expenses	1,033
Net cash provided by operating activities	18,402
Cash Flows from Investing Activities:	
Acquisition of subsidiaries, net of cash acquired	(12,615)
Proceeds from sales of available-for-sale securities	10
Acquisition of property, plant and equipment	(1,874)
Net cash used in investing activities	(14,479)
Cash Flows from Financing Activities:	
Purchase of treasury stock	(267)
Issuance of treasury stock	196
Dividends paid	(1,036)
Proceeds from exercise of stock options	572
Principal payments of long-term debt and notes payable	(1,198)
Net cash provided by (used in) financing activities	(1,733)
Effect of exchange rate changes in cash	(217)
Net increase in cash and cash equivalents	1,973
Cash and cash equivalents at beginning of period	31,029
Cash and cash equivalents at end of period	$ 33,002
Supplemental disclosures of cash flow information:	
Cash paid during the six months for:	
Interest	$ 84

Income taxes	198

(See Notes to Consolidated Financial Statements)

VITAL SIGNS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. The consolidated balance sheet as of March 31, 2002, the consolidated statements of income for the three and six months ended March 31, 2002 and 2001 and the consolidated statement of cash flows for the six months ended March 31, 2002 and 2001 have been prepared by Vital Signs, Inc. (the "Company" or "VSI") and are unaudited. In the opinion of management, all adjustments (consisting solely of normal recurring adjustments) necessary to present fairly the financial position at March 31, 2002 and the results of operations for the three-month and six-month periods ended March 31, 2002 and 2001 and cash flows for the six-month periods ended March 31, 2002 and 2001 have been made.

2. See the Company's Annual Report on Form 10-K for the year ended September 30, 2001 (the "Form 10-K") for additional disclosures relating to the Company's consolidated financial statements.

3. The Company adopted Statement of Financial Accounting Standards No. 131 "Disclosures about Segments of an Enterprise and Related Information" at September 30, 1999. The Company designs, manufactures and distributes single-use medical products. The Company's other business segments do not meet the criteria for separate disclosures.

4. At March 31, 2002, the Company's inventory was comprised of raw materials, $13,826,000, and finished goods, $10,986,000.

5. For details of legal proceedings, see Part II, Item 1, "Legal Proceedings".

6. In June 2001, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 142 ("SFAS 142"), "Goodwill and Other Intangible Assets", which is required to be applied for fiscal years beginning after December 15, 2001. The Company has adopted SFAS 142 as of October 1, 2001. SFAS 142 eliminates the amortization of goodwill and certain other intangible assets. It also requires Vital Signs to complete a test for impairment of these assets annually, as well as a transitional goodwill impairment test within six months from the date of adoption. The Company has completed this impairment test, and has found no impairment. SFAS 142 also requires disclosure of what net income would have been in all periods presented had SFAS 142 been in effect. The following table is provided to disclose what net income would have been had SFAS 142 been adopted in prior periods:

In thousands except per share amounts	FOR THE SIX-MONTHS ENDED MARCH 31, 2002	2001
Reported net income	$14,257	$11,991
Add back: goodwill amortization, net of tax	--	588
Adjusted net income	$14,257	$12,579
Basic earnings per share as reported	$ 1.11	$ .97
Adjusted basic earnings per share	1.11	1.01
Diluted earnings per share as reported	1.09	.94
Adjusted diluted earnings per share	1.09	.99

(Notes to Consolidated Financial Statements continued from previous page)

7. On January 1, 2002 the Company's National Sleep Technologies, Inc. ("NST") subsidiary completed its merger with HSI Medical Services, Inc. ("HSI"), a subsidiary of the Johns Hopkins Health System, with the merged entity to be known as Sleep Services of America, Inc. NST issued 7,921,408 shares of its Common Stock with a fair value of approximately $4,753,000, along with warrants to purchase 326,791 shares of NST's common stock in exchange for all of the outstanding common stock of HSI. The excess of the purchase price over the fair value of the net assets acquired, goodwill, was approximately $3,490,000. The Company's interest in the combined NST entity is approximately 62%. Goodwill was recognized in accordance with Statement of Financial Accounting Standards No. 142 ("Goodwill and Other Intangible Assets").

8. On March 28, 2002, the Company consummated the merger of Stelex, Inc. ("Stelex") into the Company's wholly owned subsidiary, The Validation Group, Inc. ("TVG"). The surviving entity is to be known as Stelex/TVG, Inc. The purchase price for the acquisition of Stelex was approximately $13,300,000. The purchase price was allocated to the assets acquired based on their estimated fair values. The excess of the purchase price over the fair value of the net assets acquired, goodwill, was approximately $12,657,000. Goodwill was recognized in accordance with Statement of Financial Accounting Standards No. 142 ("Goodwill and Other Intangible Assets").

9. The following unaudited proforma information presents a summary of the Company's consolidated results of operations and the Stelex and HSI business as if the acquisition had occurred on October 31, 2000:

FOR THE SIX-MONTHS

	ENDED MARCH 31,	
	2002	2001
	(IN THOUSANDS, EXCEPT PER	
Net sales and revenues	93,280	86,958
Net earnings	15,129	12,316
Basic net earnings per Common Share	1.17	0.99
Diluted net earnings per Common Share	1.16	0.97

These unaudited proforma results have been prepared for comparative purposes only and do not purport to be indicative of the results of operations which would have actually resulted had the combinations been in effect on October 1, 2000 or of future results of operations.

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ITEM 2.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Forward Looking Statements

This Quarterly Report on Form 10-Q contains, and from time to time the Company expects to make, certain forward-looking statements regarding its business, financial condition and results of operations. In connection with the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995 (the "Reform Act"), the Company intends to caution investors that there are important factors that could cause the Company's actual results to differ materially from those projected in its forward-looking statements, whether written or oral, made herein or that may be made from time to time by or on behalf of the Company. Investors are cautioned that such forward-looking statements are only predictions and that actual events or results could differ materially from such statements. The Company undertakes no obligation to publicly release the results of any revisions to its forward-looking statements to reflect subsequent events or circumstances or to reflect the occurrence of unanticipated events.

The Company wishes to ensure that any forward-looking statements are accompanied by meaningful cautionary statements in order to comply with the terms of the safe harbor provided by the Reform Act. Accordingly, the Company has set forth a list of important factors that could cause the Company's actual results to differ materially from those expressed in forward-looking statements or predictions made herein and from time to time by the Company. Specifically, the Company's business, financial condition, liquidity and results of operations could be materially different from such forward-looking statements and

predictions as a result of (i) cost containment pressures on hospitals and competitive factors that could affect the Company's primary markets, including the results of competitive bidding procedures implemented by group purchasing organizations and/or the success of the Company's sales force, (ii) slow-downs in the healthcare industry or interruptions or delays in manufacturing and/or sources of supply, (iii) the Company's ability to develop or acquire new and improved products and to control costs, (iv) market acceptance of the Company's new products, (v) technological change in medical technology, (vi) the scope, timing and effectiveness of changes to manufacturing, marketing and sales programs and strategies, (vii) intellectual property rights and market acceptance of competitors' existing or new products, (viii) adverse determinations arising in the context of regulatory matters or legal proceedings (see Part II, Item 1 of this Quarterly Report on Form 10-Q), (ix) healthcare industry consolidation resulting in customer demands for price concessions, (x) the reduction of medical procedures in a cost conscious environment, (xi) efficacy or safety concerns with respect to marketed products, whether scientifically justified or not, that may lead to product recalls, withdrawals or declining sales, and (xii) healthcare reform and legislative and regulatory changes impacting the healthcare market both domestically and internationally.

Results of Operations

The following table sets forth, for the periods indicated, the percentage increase of certain items included in the Company's consolidated statement of income.

	INCREASE/(DECREASE) THREE MONTHS ENDED MARCH 31, 2002 COMPARED WITH THREE MONTHS ENDED MARCH 31, 2001
Revenues	6.3%
Cost of goods sold and services performed	16.1%
Gross profit	(2.9)%
Selling, general and administrative expense	8.3%
Research and development expenses	(9.2)%
Income before provision for income taxes and minority interest in income of consolidated subsidiary	38.2%
Provision for income taxes	57.1
Net income	30.5%

COMPARISON: QUARTER ENDED MARCH 31, 2002
AND QUARTER ENDED MARCH 31, 2001

Net sales and revenues for the quarter ended March 31, 2002 increased by $2,585,000 or 6.3% compared with the same period last year. The increase was primarily due to the growth within the Company's sleep companies, Breas Medical and Sleep Services of America, and the growth in the anesthesia business.

Sales of anesthesia products, representing 39.2% of net sales and revenues, increased by approximately $1,498,000 or 9.6% from the quarter ended March 31, 2001 due primarily to volume growth in anesthesia circuit sales led by the Company's new anesthesia breathing circuit Limb-O'TM'. Sales of respiratory/critical care products, representing 37.0% of net sales and revenues, decreased by approximately $1,791,000 or 10.0%, primarily due to the loss of a major customer by the Company's validation consulting service company. Sales by the Company's sleep service companies, representing 23.8% of net sales and revenues, increased by $2,878,000, or 38.7% due primarily to a growth in sales of the Company's Breas subsidiary, and the merger of NST with HSI, effective January, 1, 2002.

The Company's reported gross profit percentage for the quarter ended Mach 31, 2002 was 47.0% compared to 51.4% in the same time period of the last fiscal year. The decrease in gross profit percentage is primarily due to a re-evaluation of the carrying value of the Company's inventory. The inventory reserve balance was increased by approximately $1,500,000 and additional reserves of approximately $400,000 were established for product costs relating to sales returns. Adjusting for these events the Company's gross profit percentage for the quarter ended March 31, 2002 would have been 51.3%

Selling, general and administrative expenses (S, G & A) for the quarter ended March 31, 2002 increased by $870,000 or 8.3% over the prior year's quarter primarily due to additional employees resulting from the merger of NST and HSI, and an increase of approximately $200,000 in the provision for doubtful accounts for certain international receivables and an increase of approximately $190,000 in legal accruals.

Research and development expenses ("R&D") decreased by $189,000 due to reduced expenditures on R & D projects.

Other income, net of other expense, (including interest income and expense) for the quarter ended March 31, 2002, decreased by $622,000 from the prior year's quarter primarily due to the benefit in the quarter ended March 31, 2001 of a foreign currency translation gains, and reduced interest income in the quarter ended March 31, 2002 resulting from lower interest rates available.

During the quarter ended March 31, 2002, the Company reversed $5.0 million in litigation accruals as a result of the successful conclusion of a patent infringement action filed in Japan. See "Legal Proceedings".

The Company's effective tax rates were 34.1% and 30.0% for the quarters ended March 31, 2002 and 2001, respectively. The increase in the effective tax

rate is related to an increase in the tax rate and subsequently the tax expense at our Breas operation.

COMPARISON: SIX MONTHS ENDED MARCH 31, 2002
AND SIX MONTHS ENDED MARCH 31, 2001

Net sales and revenues for the six months ended March 31, 2002 increased by $4,086,000 or 5.0% compared with the same period last year. The increase was primarily due to the growth within the Company's sleep companies, Breas and Sleep Services of America, and the growth in the anesthesia business.

Sales of anesthesia products, representing 41.6% of net sales and revenues, increased by approximately $3,098,000 or 9.6% from the six-month period ended March 31, 2001 due primarily to volume growth in anesthesia circuit sales led by the Company's new anesthesia breathing circuit Limb-O'TM'. Sales of respiratory/critical care products, representing 36.9% of net sales and revenues, decreased by approximately $2,650,000 or 7.7% primarily due to the loss of a major customer by the Company's validation service company. Sales by the Company's sleep service companies, representing 21.5% of net sales and revenues, increased by $3,638,000, or 24.6% due primarily to a growth in sales of the Company's Breas subsidiary and the merger of NST with HSI to form Sleep Services of America, effective January, 1, 2002.

The Company's reported gross profit percentage for the six months ended March 31, 2002 was 49.1% compared to 51.5% in the same time period of the last fiscal year. The decrease in gross profit percentage is primarily due to the to a re-evaluation of the carrying value of the Company's inventory. The inventory reserve balance was increased by approximately $1,500,000 and additional reserves of approximately $400,000 were established for product costs relating to sales returns and rebates. Adjusting for these events, the Company's gross profit percentage would have been equivalent to the prior year at 51.3%.

Selling, general and administrative expenses (S, G & A) increased by $1,097,000 or 5.3% primarily due to additional employees resulting from the merger of NST and HSI, and an increase of approximately $200,000 in the provision for doubtful accounts for certain international receivables and an increase of approximately $190,000 in legal accruals.

Research and development expenses ("R&D") decreased by $160,000 or 4.2% due to reduced expenditures on R & D projects.

Other income, net of other expense, (including interest income and expense) for the six-month period ended March 31, 2002, decreased by $215,000 from the prior year's quarter primarily due to the benefit in the six months ended March 31, 2001 of a foreign currency translation gains, and reduced interest income during the six months ended March 31, 2002 resulting from lower interest rates available and a reduction in the amount of contributions.

During the quarter ended March 31, 2002, the Company reversed $5.0 million in litigation accruals as a result of the successful conclusion of a

patent infringement action filed in Japan. See "Legal Proceedings".

The Company's effective tax rates were 33.8% and 30.1% for the six month period ended March 31, 2002 and 2001 respectively. The increase in effective tax rate over the prior year's six-month period reflects an increase in taxable income.

Liquidity and Capital Resources

The Company continues to rely upon cash flow from its operations. During the six-month period ended March 31, 2002, cash and cash equivalents increased by approximately $1,973,000. The increase was primarily due to net cash provided by operations of approximately $18.4 million and the proceeds from the exercise of stock options of $0.6 million. These increases were partially offset by cash used for the acquisition of Stelex, Inc. of approximately $12.6 million, net of cash acquired; capital expenditures of approximately $1.9; dividend payments of approximately $1.0 million; and principal payments on notes payable and debt of approximately 1.2 million. The combined total of cash and cash equivalents and long-term marketable securities was approximately $33.4 million at March 31, 2002 as compared to $31.5 million at September 30, 2001.

At March 31, 2002, the Company had approximately $33,002,000 in cash and cash equivalents. On that date, the Company's working capital was $74,115,000 and the current ratio was 3.7 to 1, as compared to $70,493,000 and 3.5 to 1 at September 30, 2001.

Capital expenditures of approximately $1.9 million for the six-month period primarily reflected the buy-out of its operating lease for the fair market value of the Company's Colorado plant equipment and the purchase of a packaging line for that facility.

The Company's current policy is to retain working capital and earnings for use in its business, subject to the payment of certain cash dividends and treasury stock repurchases. Such funds may be used for product development, product acquisitions and business acquisitions, among other things. The Company regularly evaluates and negotiates with domestic and foreign medical device companies regarding potential business or product line acquisitions or licensing arrangements by the Company.

The Company has a $25 million line of credit with Chase Manhattan Bank ("Chase"). Chase has also expressed its intention to provide additional funds for the Company's future acquisitions, provided that each such acquisition meets certain criteria. The terms for any borrowing would be negotiated at the date of origination. There were no amounts outstanding at March 31, 2002.

Management believes that the funds generated from operations, along with the Company's current working capital position and available bank credit, will be sufficient to satisfy the Company's capital requirements for the foreseeable future. This statement constitutes a forward-looking statement under the Reform Act. The Company's liquidity could be adversely impacted and its need

for capital could materially change if costs are higher than anticipated, the Company were to undertake acquisitions demanding significant capital, operating results were to differ significantly from recent experience or adverse events were to affect the Company's operations.

ITEM 3.

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company is exposed to market risks, including the impact of commodity price changes and changes in the market value of its investments and, to a lesser extent, interest rate changes and foreign currency fluctuations. In the normal course of business as described below, the Company employs policies and procedures with the objective of limiting the impact of market risks on earnings and cash flows and to lower its overall borrowing costs.

The Company believes that the impact of interest rate changes and foreign currency fluctuations is not material to the Company's financial condition. The Company does not enter into interest rate and foreign currency transactions for speculative purposes. It is also the Company's policy to price products from vendors and to customers in U.S. dollars and to receive payment in U.S. dollars. Historically, the international portion of the Company's sales has been relatively small and the effect of changes in interest rates and foreign exchange rates on the Company's earnings generally has been small relative to other factors that also affect earnings, such as unit sales and operating margins. However, the international segment is expected to grow both in terms of actual sales and as a percentage of the Company's total sales and the Company may in the future need to revise or change its approach to managing interest rate and foreign currency transactions.

The Company's risks involving commodity price changes relate to prices of raw materials used in its operations. The Company is exposed to changes in the prices of latex and various plastics and resins for the manufacture of its products. The Company does not enter into commodity futures or derivative instrument transactions. Except with respect to its single source for face masks, it is the Company's policy to maintain commercial relations with multiple suppliers and when prices for raw materials rise to attempt to source alternative supplies.

Subsequent Events

On May 1, 2002, the Board of Directors terminated the Company's previously announced buy-back program, under which the Company acquired a total of 61,000 shares of Common Stock since the inception of the program in February, 2002.

In April 2002, the Company paid approximately $8.2 million in cash to settle liabilities relating to the purchase of the remaining shares in Breas Medical, AB. The Company now owns 100% of Breas Medical, AB.

PART II.
Other Information

ITEM 1.

Legal Proceedings:

(a) Reference is made to Item 3 of the Company's Annual Report on Form 10-K for the year ended September 30, 2001.

(b) In September 1996, a patent infringement action was filed in Japan against an OEM medical device distributor in connection with the sale in Japan of Marquest Medical Products, Inc.'s ABG syringe product line. In July 1999 the Court indicated at a hearing that, based on one exhibit submitted by the plaintiff, the Marquest ABG syringe products appeared to infringe the plaintiff's patent, and requested that the plaintiff submit an updated proof of damages. In July 1999, plaintiff filed an updated proof of damages of approximately $6.5 million, plus interest and costs. On June 23, 2000 the Court entered a judgment against the Company's distributor for Yen 336,872,689 ($2,887,645) plus five percent annual interest. The distributor (which has patent indemnification protection from the Company's Marquest subsidiary) appealed the judgment to the Tokyo Supreme Court. On March 28, 2002, the appellate court ruled in favor of the distributor, thereby ending the litigation and ending the Company's exposure with respect to this proceeding.

(c) On December 6, 1999 a complaint was filed against the Company on behalf of the former shareholders of Vital Pharma, Inc. ("VPI") alleging breach of contract for failure to pay earnout payments allegedly due under the stock purchase agreement for the sale of VPI in December, 1995. The Company answered the complaint, filed counter-claims and moved to transfer the case to arbitration. In August, 2000 the court ordered plaintiff to submit such claims to binding arbitration and stayed all other proceedings pending the outcome of the arbitration. The matter is in the discovery phase before the arbitrator. Notwithstanding an order by the arbitrator to complete discovery by April, 2002, the only discovery which has taken place has been the exchange of documents. The remainder of discovery is expected to be completed by the end of the current fiscal year.

The Company is also involved in other legal proceedings arising in the ordinary course of business.

The Company cannot predict the outcome of its legal proceedings with certainty. However, based upon its review of pending legal proceedings, the Company does not believe the ultimate disposition of its pending legal proceedings will be material to its financial condition. Predictions regarding the impact of pending legal proceedings constitute

forward-looking statements under the Reform Act. The actual results and impact of such proceedings could differ materially from the impact anticipated, primarily as a result of uncertainties involved in the proof of facts in legal proceedings.

ITEM 6.

Exhibits and Reports on Form 8-K

A) A Current Report on Form 8-K was filed on April 8, 2002, announcing (under Item 5) the Company's acquisition of Stelex, Inc.

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 thereunto duly authorized.

VITAL SIGNS, INC.

By: /s/ Joseph F. Bourgart

Joseph F. Bourgart
Executive Vice President and
Chief Financial Officer

Date: May 15, 2002

STATEMENT OF DIFFERENCES

The trademark symbol shall be expressed as............................ 'TM'