UNITED STATES
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 June 30, 2003

OR

o 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 000-30713

Intuitive Surgical, Inc.

(Exact name of Registrant as specified in its Charter)

Delaware	**77-0416458**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification Number)

950 Kifer Road
Sunnyvale, California 94086
(Address of Principal Executive Offices including Zip Code)

(408) 523-2100
(Registrant's Telephone Number, Including Area Code)

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 reports), and (2) has been subject to such filing requirements for the past 90 days. YES x NO o

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). YES x NO o

The Registrant had 26,692,575 shares of Common Stock, $0.001 par value per share, outstanding as of July 31, 2003.

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PART I -- FINANCIAL INFORMATION

Item 1. Financial Statements

INTUITIVE SURGICAL, INC.
CONSOLIDATED BALANCE SHEETS
(IN THOUSANDS, EXCEPT SHARE DATA)

	June 30, 2003 (Unaudited)	December 31, 2002 (See Note 1)
ASSETS		
Current assets:		
Cash and cash equivalents	$ 17,681	$ 17,607
Short-term investments	25,169	33,232
Accounts receivable	21,855	16,887
Inventory, net	13,601	8,738
Prepaid expenses	2,046	2,161
Total current assets	80,352	78,625
Property and equipment, net	11,630	10,388
Intangible and other assets	10,843	2,568
Goodwill	142,658	--
Total assets	245,483	91,581
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 17,204	$ 9,282
Accrued compensation and employee benefits	5,282	4,666
Warranty accrual	2,005	2,269
Restructuring accrual	3,444	--
Other accrued liabilities	2,485	3,497
Deferred revenue	7,131	4,838
Current portion of notes payable	1,244	1,511

Total current liabilities	38,795	26,063
Long-term notes payable	1,235	1,838
Deferred revenue	877	--
Commitments and contingencies	--	--
Stockholders' equity:		
Common stock, 100,000,000 shares authorized, $0.001 par value, 26,643,541 and 18,357,513 shares issued and outstanding as of June 30, 2003 (see Note 3) and December 31, 2002, respectively	27	36
Additional paid-in capital	334,162	191,020
Deferred compensation	(434)	(223)
Accumulated deficit	(130,206)	(128,791)
Accumulated other comprehensive income	1,027	1,638
Total stockholders' equity	204,576	63,680
Total liabilities and stockholders' equity	$ 245,483	$ 91,581

See accompanying notes to condensed consolidated financial statements.

INTUITIVE SURGICAL, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)
(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2003	2002	2003	2002
Sales:				
Products	$ 19,231	$ 18,243	$ 36,666	$ 31,700
Services	2,222	1,144	4,022	2,096
Total sales	21,453	19,387	40,688	33,796
Cost of sales:				
Products	6,906	8,440	14,677	15,167
Services	1,000	785	1,967	1,565
Total cost of sales	7,906	9,225	16,644	16,732
Gross profit	13,547	10,162	24,044	17,064
Operating costs and expenses:				
Selling, general and administrative	9,389	9,784	19,598	18,569
Research and development	3,627	4,645	7,050	8,877
Total operating costs and expenses	13,016	14,429	26,648	27,446
Income (loss) from operations	531	(4,267)	(2,604)	(10,382)
Other income, net	347	527	1,189	1,025
Net income (loss)	$ 878	$ (3,740)	$ (1,415)	$ (9,357)
Net earnings (loss) per share:				
Basic	$ 0.05	$ (0.21)	$ (0.08)	$ (0.51)
Diluted	$ 0.05	$ (0.21)	$ (0.08)	$ (0.51)
Shares used in computing net earnings (loss) per share:				
Basic	18,580	18,192	18,506	18,173
Diluted	18,973	18,192	18,506	18,173

See accompanying notes to condensed consolidated financial statements.

INTUITIVE SURGICAL, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)
(IN THOUSANDS)

	For the Six Months Ended June 30,	
	2003	2002
OPERATING ACTIVITIES:		

Net loss	$ (1,415)	$ (9,357)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation	1,777	1,409
Loss on sales of fixed assets	5	64
Amortization of deferred compensation and stock compensation	296	395
Amortization of intangible and other assets	495	390
Changes in operating assets and liabilities, net of operating assets and liabilities:		
Accounts receivable	(493)	(1,965)
Prepaid expenses	384	1,429
Inventory	(191)	(1,048)
Other assets	(827)	--
Accounts payable	30	(267)
Accrued compensation and employee benefits	(1,443)	969
Warranty accrual	(564)	363
Other accrued liabilities	(2,012)	1,447
Accrued royalty expense	--	(1,000)
Deferred revenue	944	(164)
Net cash used in operating activities	(3,014)	(7,335)
INVESTING ACTIVITIES:		
Acquisition of property and equipment	(1,030)	(4,805)
Disposition of property and equipment	1	62
Acquisition of business, net of cash acquired	(4,088)	--
Purchase of short-term investments	(2,934)	(8,491)
Proceeds from sales of short-term investments	5,444	21,216
Proceeds from maturities of short-term investments	5,097	12,108
Net cash provided by investing activities	2,490	20,090
FINANCING ACTIVITIES:		
Proceeds from issuance of common stock	1,629	1,089
Repurchase of common stock	(6)	(1)
Proceeds from notes payable	--	950
Repayment of notes payable	(870)	(1,359)
Net cash provided by financing activities	753	679
Foreign currency translation adjustments	(155)	(49)
Net increase in cash and cash equivalents	74	13,385
Cash and cash equivalents, beginning of period	17,607	10,487
Cash and cash equivalents, end of period	$ 17,681	$ 23,872
Non-cash investing activity:		
Common stock issued in connection with acquisition of business	$ 141,437	$ --

See accompanying notes to condensed consolidated financial statements.

INTUITIVE SURGICAL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

In this report, "Intuitive Surgical," "Intuitive," and the "Company" refer to Intuitive Surgical, Inc.

NOTE 1. BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and notes required by accounting principles generally accepted in the United States for complete financial statements. In the opinion of management, all normal, recurring adjustments considered necessary for a fair presentation have been included. The consolidated balances at December 31, 2002 were derived from the audited financial statements included in Intuitive Surgical, Inc.'s Annual Report on Form 10-K/A for the year ended December 31, 2002 (the "Annual Report"). The financial statements should be read in conjunction with the audited financial statements for the year ended December 31, 2002, included in the Annual Report. The results for the interim period ended June 30, 2003 are not necessarily indicative of the results to be expected for the full year ending December 31, 2003 or future operating periods.

On June 30, 2003, Intuitive Surgical acquired Computer Motion, Inc. through the merger of Computer Motion with a wholly owned subsidiary of Intuitive Surgical. In the merger, each outstanding share of Computer Motion common stock was converted into 0.51426943 shares of Intuitive Surgical common stock and Intuitive Surgical assumed all of Computer Motion's outstanding options and warrants based on the same ratio, see "Note 3: Acquisition of Computer Motion, Inc."

The operations of Computer Motion, Inc. have been excluded from the accompanying unaudited condensed consolidated statements of operations for the three and six months ended June 30, 2003 and statements of cash flows for the six months ended June 30, 2003 as the acquisition was not consummated until June 30, 2003.

NOTE 2. CONCENTRATIONS OF RISK

Financial instruments which subject the Company to potential risk consist of its cash equivalents, short-term investments, accounts receivable, and foreign exchange contracts. The counterparties to the agreements relating to the Company's investment securities and foreign exchange contracts consist of various major corporations and financial institutions of high credit standing. The Company believes the financial risks associated with these financial instruments are minimal.

For the six months ended June 30, 2003 and 2002, no customer accounted for more than 10% of total sales. The Company extends reasonably short collection terms but does not require collateral. The Company provides reserves for potential credit losses but has not experienced significant losses to date.

The Company's *da Vinci* Surgical System, related instruments and accessories and service accounted for all of the Company's sales for the three months and six months ended June 30, 2003 and 2002. Purchases of key parts and components used to manufacture the Company's products are from limited supply sources. The inability of any of these suppliers to fulfill the Company's supply requirements may negatively impact future operating results.

The Company operates in one segment, the development and marketing of products designed to provide the flexibility of open surgery while operating through ports. For the three months ended June 30, 2003, U.S. and international sales accounted for 70% and 30%, respectively, of total sales. For the three months ended June 30, 2002, U.S. and international sales accounted for 80% and 20%, respectively, of total sales.

NOTE 3. ACQUISITION OF COMPUTER MOTION, INC.

On June 30, 2003, the Company acquired all of the outstanding shares of Computer Motion, Inc. through a merger with a wholly owned subsidiary of Intuitive Surgical. In the merger, each outstanding share of Computer Motion common stock has converted into 0.51426943 shares of Intuitive Surgical common stock and Intuitive Surgical assumed all of Computer Motion's outstanding options and warrants to purchase Computer Motion common stock based on the same ratio. The acquisition of Computer Motion is intended to enhance the Company's combined competitive position in key industries, while strengthening its work force. It also eliminated ongoing intellectual property litigation between the two companies. The acquisition is intended to enable the Company to focus on strategic products and customers, achieve significant cost synergies and economies of scale and improve results of its combined application of robotics to minimally invasive surgery bringing benefits to patients, surgeons and medical centers throughout the world. The exchange ratio in the acquisition was derived from estimates of future revenue and earnings of the combined company, in addition to measuring the relative ownership of the combined company implied by their contributions. The purchase price of this acquisition was $148.6 million resulting from the issuance to Computer Motion stockholders the right to receive approximately 8.0 million shares of Intuitive Surgical common stock on June 30, 2003, after giving effect to the 1-for-2 stock reverse split effected on July 1, 2003 (the "Reverse Split), with a fair value of approximately $125.7 million, the assumption of options and warrants to purchase approximately 2.2 million shares of Intuitive Surgical common stock, after giving effect to the Reverse Split, with a Black-Scholes fair value of approximately $15.7 million, the funding of Computer Motion's second quarter operations through a working capital loan $5.3 million, and estimated direct transaction costs of $1.8 million. The fair value of the Company's common stock was derived using an average market price per share of the Company common stock of $7.82, which was based on the closing prices for a range of trading days prior to and including the date of the acquisition, June 30, 2003 (June 24, June 25, June 26, June 27, and June 30). The measurement date for this transaction was the June 30, 2003 closing date, as the number of shares to be issued to Computer Motion stockholders was not fixed until that date.

In accordance with SFAS No. 141, the Company allocated the purchase price of the acquisition to the tangible assets, liabilities and intangible assets acquired, including in-process research and development, "IPR&D," based on their estimated fair values. The excess purchase price over those fair values is recorded as goodwill. The fair value assigned to intangible assets acquired is based on valuations prepared by independent third party appraisal firms using preliminary estimates and assumptions provided by management. The goodwill recorded as a result of the acquisition is not expected to be deductible for tax purposes. In accordance with SFAS No. 142, goodwill and purchased intangible assets with indefinite useful lives acquired after June 30, 2001 are not amortized but will be reviewed at least annually for impairment. Purchased intangible assets with finite lives are amortized on a straight-line basis over their respective useful lives.

The total purchase price was comprised of the following (in thousands):

Value of Intuitive Surgical common stock issued....	$ 125,734
Assumption of Computer Motion warrants and options.	15,703
Total value of Intuitive Surgical securities.....	141,437
Direct transaction costs.....	1,827
Bridge loan facility.....	5,302
Total estimated purchase price.....	$ 148,566

The following purchase price allocation is preliminary, as future business results may differ from inherent estimates contained in the allocation, including employee severance costs, obligations related to exiting lease commitments, and other underlying assumptions. The total purchase price of has been allocated as follows (in thousands):

Cash and cash equivalents.....	$ 1,214
Accounts receivable, net.....	4,476
Inventories, net.....	4,672
Prepaid and other assets.....	269
Property, plant, and equipment.....	1,995
Other assets.....	70
Amortizable intangible assets:.	
Customer relationships.....	1,300
Developed and core technology.....	6,800
Trademark.....	200
Internal use software.....	300
In-process research and development...	100
Goodwill.....	142,658
Accounts and notes payable.....	(7,892)
Restructuring accrual.....	(3,444)
Other accrued liabilities.....	(2,361)
Deferred revenue.....	(2,225)
Deferred compensation.....	434
Total purchase price.....	$ 148,566

Goodwill

Of the total purchase price, $142.7 million was allocated to goodwill. Goodwill represents the excess of the purchase price over the fair value of the underlying net tangible and intangible assets. Goodwill is not deductible for tax purposes. In accordance with Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets," goodwill will not be amortized, but instead will be tested for impairment at least annually (more frequently if certain indicators are present). In the event management determines that goodwill has been impaired, the Company will incur an accounting charge for the impairment during the fiscal quarter in which the determination is made. (See Note 7.)

Amortizable Intangible Assets

Of the total purchase price, approximately $8.6 million was allocated to amortizable intangible assets, comprised of developed technology of $3.5 million, core technology of $3.3 million, customer relationships of $1.3 million, and other intangible assets totaling $0.5 million.

Developed technology, which comprises products that have reached technological feasibility, includes most of Computer Motion's current products, including Aesop, Zeus, Socrates, and Hermes. The balance of developed technology will be amortized on a straight-line basis over a period of seven years, representing the weighted average of the remaining product lives of the developed technology.

Core technology represents the value of patents, processes, and trade secrets, including certain designs and product features that Intuitive may integrate into future products. Core technology will be amortized on a straight-line basis over a period of seven years.

Customer relationships represent the value of Computer Motion's relationships with existing customers and is valued based upon the fair value of future business with these customers. Customer lists and other intangible assets will be amortized on a straight line basis over a period of approximately seven years. (See Note 7.)

In-process research and development

Of the total purchase price, $0.1 million was allocated to in-process research and development. Projects which qualify as IPR&D represent those that have not yet reached technological feasibility and for which no future alternative uses exist. IPR&D has been immediately, fully amortized into Intuitive Surgical's results for the three months ended June 30, 2003.

Deferred Compensation

Of the total purchase price, $0.4 million was allocated to deferred compensation for unvested options assumed, which represents the intrinsic value of unvested stock options for employees and fair value for non- employee. Deferred compensation will be amortized into expense over a three-year period using the graded vesting method.

Restructuring charges

Upon the consummation of the acquisition of Computer Motion, Intuitive's management approved plans to restructure the operations of the combined entity. The current restructuring plan provides for the elimination of redundant activities and infrastructure and will result in eliminating approximately 150 employees, or 75%, of the Computer Motion positions over the next six months with immediate severance payment. The plan includes vacating and subleasing 78% of the leased space in Goleta, California, consolidating European operations into a single site, and closing Computer Motion's Asia office,and transitioning to the Intuitive distribution sales model for the area. The Company will have a single sales and marketing organization and consolidate all manufacturing and administrative functions in Sunnyvale, California. Based upon this plan, the Company has recorded a $3.4 million accrual in accordance with EITF Issue 95-3 (EITF 95-3), "Recognition of Liabilities in Connection with a Purchase Business Combination." In accordance with EITF 95-3, the restructuring accrual has been recorded as a component of the purchase price. The accrual is comprised of $2.6 million for employee severance costs and $0.8 million to exit existing lease commitments, based upon total future lease commitments for facilities to be vacated of $2.6 million, offset by subleasing proceeds of $1.8 million. The Company has estimated vacancy periods of between 1 month and 3 years between exiting various sites and realizing subleasing proceeds.

Pro forma results of operations

The following unaudited pro forma financial information for the three and six months ended June 30, 2003 and June 30, 2002 give effect to the proposed merger of Intuitive Surgical and Computer Motion as if it had occurred on January 1, 2003 and January 1, 2002, respectively. The unaudited pro forma financial information is not intended to represent or be indicative of the consolidated results of operations that Intuitive would have reported had the acquisition been completed as of the dates presented, and should not be taken as representative of the future consolidated results or financial position of Intuitive Surgical.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2003	2002	2003	2002
Sales	$ 25,297	$ 23,969	$ 51,098	$ 43,803
Net loss	$ (10,357)	$ (10,114)	$ (21,868)	$ (21,197)
Net loss per share	$ (0.39)	$ (0.45)	$ (0.88)	$ (0.96)

NOTE 4. CASH AND CASH EQUIVALENTS

Intuitive Surgical considers all highly liquid investments with an original maturity from date of purchase of 90 days or less to be cash equivalents for the purpose of balance sheet and statement of cash flows presentation. The carrying value of cash and cash equivalents approximates market value at June 30, 2003 and December 31, 2002.

NOTE 5. SHORT-TERM INVESTMENTS

All short-term investments are classified as available- for-sale, and therefore, are carried at fair market value. The Company views its available-for-sale portfolio as available for use in its current operations. Accordingly, all investments are classified as short-term, even though the stated maturity date may be one year or more beyond the current balance sheet date. Available-for-sale securities are stated at fair market value based upon quoted market prices of the securities. Unrealized gains and losses on such securities are reported as a separate component of stockholders' equity. Realized gains and losses on available-for-sale securities, together with amortization of premiums and discounts on debt securities, are included in interest income. The cost of securities sold is based on the specific identification method. Interest and dividends on securities classified as available-for-sale are included in interest income.

NOTE 6. INVENTORY

Inventory consists of the following (in thousands):

	June 30, 2003	December 31, 2002
Raw materials	$ 4,018	$ 3,420
Work-in-process	3,312	780
Finished goods	6,271	4,538
	$ 13,601	$ 8,738

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NOTE 7. GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill represents the excess of the purchase price over the fair value of the underlying net tangible and intangible assets. In accordance with Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets," goodwill and intangible assets with indefinite useful lives can no longer be amortized; however, they will be tested for impairment at least annually (more frequently if certain indicators are present). Intangible assets with finite useful lives will continue to be amortized over their respective useful lives. In the event management determines that goodwill has been impaired, the Company will incur an accounting charge for the impairment during the fiscal quarter in which the determination is made. Of the total purchase price, $142.7 million was allocated to goodwill and $8.6 million was allocated to amortizable intangible assets, comprised of developed technology of $3.5 million, core technology of $3.3 million, customer relationships of $1.3 million, and other intangible assets totalling $0.5 million.

Other purchased intangible assets represent patents which are carried at cost less accumulated amortization. Amortization is computed using the straight-line method over the expected useful life of six or seven years. At June 30, 2003, gross intangible assets totaled $13.4 million and related accumulated amortization was $2.6 million.

NOTE 8. COMPREHENSIVE INCOME (LOSS)

The components of comprehensive income (loss) consist of the following (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2003	2002	2003	2002
Net income (loss)	$ 878	$ (3,740)	$ (1,415)	$ (9,357)
Other comprehensive income (loss):				
Foreign currency translation adjustments	(64)	(91)	(155)	(49)
Change in unrealized gain (loss) on available-for-sale securities	(15)	659	(456)	158
Comprehensive income (loss)	$ 799	$ (3,172)	$ (2,026)	$ (9,248)

The components of accumulated other comprehensive loss were as follows (in thousands):

	June 30, 2003	December 31, 2002
Accumulated net unrealized gain on available-for-sales securities	$ 1,167	$ 1,623
Foreign currency translation adjustments	(140)	15
Total accumulated other comprehensive income	$ 1,027	$ 1,638

NOTE 9. NET INCOME (LOSS) PER SHARE

The following table presents the computation of basic and diluted net income (loss) per share (in thousands, except share and per share data):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2003	2002	2003	2002
Numerator used for basic and diluted net earnings (loss) per common share	$ 878	$ (3,740)	$ (1,415)	$ (9,357)
Denominator used for basic and diluted net earnings (loss) per common share:				
Weighted-average shares outstanding	18,584,894	18,206,725	18,511,514	18,188,968
Less weighted-average shares subject to repurchase	(4,758)	(15,284)	(5,863)	(16,252)
Weighted-average shares used in computing basic common share	18,580,136	18,191,441	18,505,651	18,172,716
Add common stock equivalents	392,593	--	--	--
Weighted-average shares used in computing diluted common share	18,972,729	18,191,441	18,505,651	18,172,716
Net earnings (loss) per common share:				
Basic	$ 0.05	$ (0.21)	$ (0.08)	$ (0.51)
Diluted	$ 0.05	$ (0.21)	$ (0.08)	$ (0.51)

Common stock equivalents consisting of stock options and warrants (calculated using the treasury stock method) have been excluded from the computation of diluted net loss per share for the three months ended June 30, 2002 and the six months ended June 30, 2003 and 2002, as their inclusion would be anti- dilutive.

NOTE 10. PRODUCT WARRANTY PROVISIONS

The Company's standard policy is to warrant all shipped systems against defects in design, materials and workmanship by replacing failed parts during the first year of ownership. The Company's estimate of costs to service the warranty obligations is based on historical experience and current product performance trends.

These costs are included in cost of goods sold at the time revenue is recognized. The warranty provision is reduced by material and labor costs used for replacement activities over the warranty period. A review of the obligations is performed regularly to determine the adequacy of the reserve. Based on the outcome of this review, revisions to the estimated warranty liability are recorded as appropriate.

The following table reconciles the changes to the product warranty liability for the period indicated (in thousands):

	Balance at Beginning of Period	Warranty Usage	Warranties Expensed	Warranty Assumed in Acquisition	Balance at End of Period
Three months ended June 30, 2003..	$ 2,100	$ (337)	$ (58)	$ 300	$ 2,005
Six months ended June 30, 2003....	$ 2,269	$ (776)	$ 212	$ 300	$ 2,005

The Company from time to time enters into agreements to indemnify its customers against liability and damages arising from patent claims against the Company's product. The term of these agreements vary, but generally, a maximum obligation is not explicitly stated within the agreements. Historically, the Company has not been obligated to make any significant payments related to its customer indeminification clauses and no liabilities have been recorded for this obligation on its balance sheets as of June 30, 2003 and December 31, 2002.

NOTE 11. STOCK-BASED COMPENSATION

The Company applies Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations in accounting for its stock option plans. Accordingly, no compensation expense has been recorded for stock option grants issued with an exercise price equal to the market value of the underlying stock on the date granted. The company has recorded stock-based compensation, primarily related to deferred compensation arising from the Company's initial public offering in 2000 and plans to record stock-based deferred compensation expense related to its acquisition of Computer Motion in June 2003. Had compensation expense for the stock option grants been determined on the fair value at the grant dates consistent with the method of Statement of Financial Accounting Standards Board (SFAS) No. 123, "Accounting for Stock-Based Compensation," the Company's net loss and loss per share would have been adjusted to the pro forma amounts indicated below (amounts in thousands, except per share amounts):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2003	2002	2003	2002
Net income (loss), as reported.....	$ 878	$ (3,740)	$ (1,415)	$ (9,357)
Add: Total stock-based employee compensation expense included in reported net loss, net of $0 related tax..	141	181	296	395
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of $0 related tax effect..	(1,958)	(1,820)	(3,984)	(3,495)
Pro forma net income (loss).....	$ (939)	$ (5,379)	$ (5,103)	$(12,457)
Earnings (loss) per share:				
Basic and diluted - as reported.....	$ 0.05	$ (0.21)	$ (0.08)	$ (0.51)
Basic and diluted - pro forma.....	$ (0.05)	$ (0.30)	$ (0.28)	$ (0.69)

NOTE 12. REVERSE STOCK SPLIT

Intuitive Surgical's stockholders approved a one-for-two reverse stock split (the"Reverse Split") on June 30, 2003 and it was executed on July 1, 2003. The par value of Intuitive's common stock after the Reverse Split remained at $0.001 per shares. The rights of the holders of these securities were not otherwise modified. All shares outstanding and earnings per share information for all periods presented in these financial statements give effect to the Reverse Split. All shares, per share and market price data related to Intuitive's common shares outstanding and under employee stock plans reflect the retroactive effects of the Reverse Split.

NOTE 13. REVENUE RECOGNITION

The Company recognizes revenue when persuasive evidence of an arrangement exists, delivery has occurred or service has been rendered, the price is fixed or determinable and collectibility is reasonably assured.

In certain cases, revenue from direct system sales is generated from multiple-element arrangements which require judgment in the areas of customer acceptance, training, installation and collectibility. The Company accounts for multiple-element arrangements in accordance with the provisions of SAB 101, "Revenue Recognition in Financial Statements." Revenue is recognized as specific elements indicated in sales contracts are executed. If an element is essential to the functionality of an arrangement, the entire arrangement's revenue is deferred until that essential element is delivered. The fair value of each undelivered element that is not essential to the functionality of the system is deferred until performance or delivery occurs. The fair value of an undelivered element is based upon an estimate made by management. If an undelivered element exists, the Company will determine the fair value of the undelivered element and subtract the fair value of the undelivered element from the total consideration under the arrangement. The residual amount is recognized as the value of the delivered element. Amounts billed in excess of revenue recognized are recorded as deferred revenue on the balance sheet. Costs associated with inconsequential or perfunctory elements in multiple-element arrangements are accrued at the time of revenue recognition. The Company accounts for installation as a separate element of a multiple-element arrangement. The Company therefore recognizes the fair value of installation services upon the completion of installation.

The Company's distributors do not have price protection rights. One of the Company's distributors has return rights under limited circumstances. Such rights are accounted for under the provisions of SFAS No. 48, "Revenue Recognition When Right of Return Exists." To date, the Company has not had any system sales returns.

Revenue from sales of instruments and accessories is recognized upon shipment. Revenue related to future commitments under service contracts is deferred and recognized ratably over the service period. All costs associated with the provision of service and maintenance, including salaries, benefits, travel, spare parts and equipment, are recognized in cost of sales as incurred. Amounts billed in excess of revenue recognized are included as deferred revenue in the accompanying consolidated balance sheets.

The Company's *da Vinci* Surgical System contains a software component. The Company believes that the software element in the *da Vinci* Surgical System is an incidental part of the system. The software element within the Company's product is not sold or marketed separately to customers and the software does not operate independently of the surgical system. Furthermore, the software development effort does not require a significant cost to the Company relative to the

overall development cost of the product. As such, the software the Company provides is incidental to the surgical system as a whole and the software revenue guidance provided in SOP 97- 2 is not applicable to the Company's revenues.

NOTE 14. RECENT ACCOUNTING PRONOUNCEMENTS

In June 2002, the FASB issued SFAS 146, "Accounting for Costs Associated with Exit or Disposal Activities," which addresses accounting for restructuring, discontinued operation, plant closing, or other exit or disposal activity. SFAS 146 requires companies to recognize costs associated with exit or disposal activities when they are incurred rather than at the date of a commitment to an exit or disposal plan. The provisions of SFAS 146 are effective for exit or disposal activities that are initiated after December 31, 2002. Since SFAS 146 does not involve an entity newly acquired in a business combination, the restructuring accrual, recorded as a component of the purchase price in connection with the acquisition was established based on the provisions of EITF Issue No. 95-3, "Recognition of Liabilities in Connection with a Purchase Business Combination" and SFAS 146 did not impact the Company's results of operations or financial position during the six months ended June 30, 2003.

In January 2003, the FASB issued Interpretation No. 46, or FIN 46, "Consolidation of Variable Interest Entities." FIN 46 requires a variable interest entity to be consolidated by a company if that company is subject to a majority of the risk of loss from the variable interest entity's activities or entitled to receive a majority of the entity's residual returns or both. A variable interest entity is a corporation, partnership, trust, or any other legal structures used for business purposes that either (a) does not have equity investors with voting rights, or (b) has equity investors that do not provide sufficient financial resources for the entity to support its activities. A variable interest entity often holds financial assets, including loans or receivables, real estate or other property. A variable interest entity may be essentially passive or it may engage in research and development or other activities on behalf of another company. The consolidation requirements of FIN 46 apply immediately to variable interest entities created after January 31, 2003. FIN 46 also requires consolidation of variable interest entities entered into prior to January 31, 2003 in the first fiscal year or interim period beginning after June 15, 2003. Certain of the disclosure requirements apply to all financial statements issued after January 31, 2003, regardless of when the variable interest entity was established. The adoption of FIN 46 has not had an impact on the Company's financial position or results of operations during the six months ended June 30, 2003.

In October 2002, the Emerging Issues Task Force reached consensus on issue 00-21, or EITF 00-21, "Revenue Arrangements with Multiple Deliverables." The principles and application guidance of EITF 00-21 should be used to determine (a) how the arrangement consideration should be measured, (b) whether the arrangement should be divided into separate units of accounting, and (c) how the arrangement consideration should be allocated among the separate units of accounting. The guidance in this issue is effective for revenue arrangements entered into in fiscal periods beginning after June 15, 2003. The Company is evaluating the possible impact of the adoption of EITF 00-21 on its results of operations and financial position.

NOTE 15. CONTINGENCIES

On September 1, 2000, Brookhill-Wilk 1, LLC ("Wilk") filed a lawsuit against Intuitive Surgical in the United States District Court for the Southern District of New York (Case No. 00 Civ. 6599 (NRB)) alleging that by making, using, selling or offering for sale our *da Vinci* Surgical System, the Company is infringing U.S. Patent Nos. 5,217,003 and 5,368,015 in willful disregard of Wilk's patent rights. These patents concern methods and devices for "remote" surgery. In March 2001, Wilk withdrew its assertion of the '015 patent against the Company. On November 8, 2001, in response to a motion on one of Intuitive Surgical's noninfringement defenses, the District Court granted summary judgment of noninfringement of the '003 patent in the Company's favor and dismissed Wilk's complaint in its entirety without prejudice. Wilk appealed the summary judgment ruling to the U.S. Court of Appeals for the Federal Circuit.

On April 11, 2003, the Court of Appeals reversed the District Court's judgment and remanded the case for further proceedings. This reversal is based on the Court of Appeals' determination that the particular claim limitation at issue should be interpreted differently than as construed by the District Court. The Court of Appeals has since clarified its opinion in response to Intuitive Surgical's petition for rehearing. Upon remand, Intuitive Surgical intends to continue to vigorously defend its rights and, if necessary, is prepared to continue to dispute the meaning of other portions of the asserted claim language and to conduct discovery and file further motions on whether the patent is infringed, valid and/or enforceable. Intuitive Surgical believes that it will prevail in the litigation and that it has multiple meritorious defenses to Wilk's allegations. However, litigation is unpredictable and Intuitive Surgical may not prevail. The case remains in its early stages of discovery in the District Court.

If the Company loses Wilk's suit against us, it will hurt our competitive position, may be costly and may prevent the Company from selling its products. If the Company loses the patent suit, it may need to obtain from Wilk a license to this technology to continue to market its products that have been found to infringe Wilk's patents. This license could be expensive, which could seriously harm the Company's business. If Wilk is successful in its suit against the Company and is unwilling to grant a license, the Company may be required to stop selling its products that are found to infringe Wilk's patents unless the Company can redesign them so they do not infringe Wilk's patents, which it may be unable to do. In addition, the Company could be required to pay Wilk damages, including treble damages, which could be substantial and harm its financial position. Due to the inherent uncertainties of litigation, however, the Company cannot accurately predict the ultimate outcome of the litigation against Wilk at this time and, therefore, cannot estimate the range of possible loss.

During the second quarter 2003, two former patients of The Valley Hospital in New Jersey filed suit against The Valley Hospital, their surgeon(s) and Intuitive Surgical, Inc. alleging various harms caused during their earlier surgeries. Intuitive was named because the *da Vinci* System was utilized for a portion of the complained-of surgeries and a small portion of the tip of an *EndoWrist* instrument remained in each patient after each surgery. Each suit presents multiple claims variously alleging, among others, negligence, carelessness and/or recklessness by each defendant, that the *da Vinci* System was defectively designed and manufactured, that Intuitive failed to properly instruct and train its surgeon in its use, and that the defendants failed to properly apprise the patients of the risks involved. Each suit seeks an unspecified amount of general, special and punitive damages from the defendants, in addition to a request to recover the costs of suit and attorney fees. As each suit was just recently filed, both are in very early stages and discovery has not yet begun. Due to the inherent uncertainties of the litigation, and the early stage of this case, the Company cannot accurately predict the outcome of this litigation at this time and therefore, cannot estimate the range of possible loss.

The foregoing proceedings could be expensive to litigate, may be protracted and the Company's confidential information may be compromised. Whether or not the Company is successful in these lawsuits, these proceedings could consume substantial amounts of its financial and managerial resources. At any time, the other parties may file additional claims against the Company, or the Company may file claims against them, which could increase the risk, expense and duration of the litigations. For more information on the Company's litigation with Wilk, see "Part II-Item 1: Legal Proceedings."

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

In this report, "Intuitive Surgical," "Intuitive," the "Company," "we," "us," and "our" refer to Intuitive Surgical, Inc.

This Management's Discussion and Analysis of Financial Condition as of June 30, 2003 and Results of Operations for the three month and six month periods ended June 30, 2003 and June 30, 2002 should be read in conjunction with the Management's Discussion and Analysis of Financial Condition and Results of Operations included in our Annual Report on Form 10-K/A for the year ended December 31, 2002.

Except for historical information, the discussion in this report contains forward-looking statements that involve risks and uncertainties, such as statements of our plans, objectives, expectations, and intentions. The cautionary statements made in this report should be read as applying to all related forward-looking statements wherever they appear in this report. Our actual results could differ materially from those discussed here. Factors that could cause or contribute to these differences include those discussed in "Factors Affecting Operating Results" below as well as those discussed elsewhere.

Intuitive®, da Vinci®, InSite®, EndoWrist®, Zeus®, Hermes®, and Aesop® are registered trademarks of Intuitive Surgical, Inc.

OVERVIEW

We design, manufacture, and market the *da Vinci* Surgical System, an advanced surgical system that we believe represents a new generation of surgery-the third generation. The *da Vinci* Surgical System consists of a surgeon's console, a patient-side cart, a high performance vision system and proprietary "wristed" instruments. The *da Vinci* Surgical System seamlessly translates the surgeon's natural hand movements on instrument controls at a console into corresponding micro-movements of instruments positioned inside the patient through small puncture incisions, or ports. We believe that the *da Vinci* Surgical System is the only commercially available technology that can provide the surgeon with the intuitive control, range of motion, fine tissue manipulation capability and 3-D visualization characteristic of open surgery, while simultaneously allowing the surgeons to work through the small ports of minimally invasive surgery, or MIS. By placing computer-enhanced technology between the surgeon and the patient, we believe that the *da Vinci* Surgical System enables surgeons to perform better surgery in a manner never before experienced.

In 1999, we obtained permission from the European Union to affix the CE Mark to the *da Vinci* Surgical System and *EndoWrist* instruments for general surgical and cardiac surgical use. Based on this approval, we recognized revenue for the first time in the second quarter of 1999 for the sale of our products. In July 2000, we received clearance from the U.S. Food and Drug Administration, or FDA, to begin commercialization of our *da Vinci* Surgical System in the United States for use in laparoscopic surgical procedures. In March 2001, we received clearance from the FDA for use of our *da Vinci* Surgical System in non-cardiac thoracoscopic surgical procedures. In May 2001, we received market clearance from the FDA to promote use of the *da Vinci* Surgical System for performance of laparoscopic radical prostatectomy procedures. In November 2002, we received clearance from the FDA for use of the *da Vinci* Surgical System in thoracoscopically- assisted cardiotomy procedures. In January 2003, we began promoting atrial septal defect closure surgery under the November 2002 cardiotomy clearance.

To date, the majority of our revenues have come from the sales of the *da Vinci* Surgical System, which are high revenue dollar items. A smaller percentage of revenues have come from sales of *EndoWrist* instruments and accessories, which are lower revenue dollar items. A small percentage of revenue comes from ongoing service of installed *da Vinci* Surgical Systems. Although we expect the majority of our revenues to continue to come from the sale of *da Vinci* Surgical Systems over the next few years, we believe that the percentage of revenue from our *EndoWrist* instruments and service will continue to increase. Due to the high dollar revenue per system sold, small variations in system unit sales may cause revenue to vary significantly from quarter to quarter. During the useful life of each installed *da Vinci* Surgical System, we expect to generate recurring revenue through sales of the *EndoWrist* instruments and accessories and ongoing service. The percentage of revenue derived from recurring instrument, accessory, and service revenue has grown from 20% for the quarter ended June 30, 2002 to 30% for the quarter ended June 30, 2003.

COMPUTER MOTION ACQUISITION

On June 30, 2003, the Company acquired Computer Motion, Inc. In this transaction, Computer Motion merged with a wholly owned subsidiary of Intuitive Surgical and each share of Computer Motion common stock was converted into 0.51426943 shares of Intuitive Surgical common stock. The total purchase price of the transaction was $148.6 million compared to $113.0 million presented on a pro forma basis in the Company's Registration Statement on Form S-4 filed with the SEC in connection with the transaction (the "pro forma") as if the transaction had closed as of March 31, 2003. The increase in purchase price resulted primarily from a rise in the Intuitive Surgical common stock price from $6.20 at the April 29, 2003 measurement date in the pro forma presentation to the $7.82 value used to measure the value of stock issued at the June 30, 2003 close date. The purchase price also increased $5.3 million to reflect funds loaned to Computer Motion during the second quarter of 2003 to fund its operations. The measurement date for this transaction was the June 30, 2003 closing date, as the number of shares to be issued to Computer Motion stockholders was not fixed until that date.

The following table compares the allocation of purchase price between the pro forma financial information presented in the Form S-4 and the actual transaction:

	Actual	Pro forma
Tangible assets	$ 218	$ 10,136
Intangible assets	8,700	32,400
Restructuring accrual	(3,444)	--
Deferred compensation	434	574
Goodwill	142,658	69,854
Total purchase price	$ 148,566	$ 112,964

The tangible assets acquired were $9.9 million less than pro forma due primarily to Computer Motion's second quarter loss of $5.9 million and adjustments made to the fair value of Computer Motion's inventory and fixed asset historical balances. Intangible assets acquired were $23.7 million less than pro forma primarily due to lower developed and core technology valuations resulting from reduced business forecasts for the acquired Computer Motion Zeus product line. The restructuring accrual was recorded in the actual allocation, as management has now developed a restructuring plan with sufficient detail to record this reserve, primarily for employee severance pay and facility closure costs. Goodwill was higher than pro forma due to the combined impact of the rise in the purchase price and the changes in the other tangible and intangible assets acquired.

The current restructuring plan provides for the elimination of approximately 75% of the Computer Motion employees, exiting 78% of the space in Goleta, California, consolidating European operations into a single site, closing the Computer Motion's Asia office, and transitioning to the Intuitive distribution sales model for the area. The Company will have a single sales and marketing organization and consolidate all manufacturing and administrative functions in the Sunnyvale, California headquarters. Based on these plans, the Company projects to achieve annual pre-tax cost savings of at least $18 million to be phased in beginning in the third quarter of 2003. The Company estimates that approximately $12.0 million of those savings will result from a substantial reduction in headcount.

RESULTS OF OPERATIONS

Sales. Total sales for the three months ended June 30, 2003 were $21.5 million, up 11% from $19.4 million for the three months ended June 30, 2002. The increase in second quarter of 2003 sales was driven by continued recurring revenue growth, consisting of instruments, accessories, and service. Second quarter 2003 recurring revenue totaled $6.4 million, up $2.6 million over the prior year and up $1.0 million sequentially over the first quarter of this year. Higher recurring revenue was driven by growth in the installed base of *da Vinci* Surgical Systems and surgical procedures performed with the system. We shipped 14 *da*

Vinci Surgical Systems during the second quarter of 2003, compared to 16 in the second quarter of 2002. During the second quarter 2003, we launched our fourth arm product, shipping 9 units during the quarter. Overall, second quarter 2003 system revenue was down slightly to $15.1 million, compared to $15.6 million for the second quarter of 2002. As of June 30, 2003, there were 177 cumulative *da Vinci* Surgical Systems shipped, compared to 118 as of June 30, 2002.

On a year to date basis, total sales for the six months ended June 30, 2003 were $40.7 million, up 20% from $33.8 million for the six months ended June 30, 2002. The increase was driven by continued growth in recurring revenue. Sales of instruments, accessories and service grew to $11.8 million for the first half of 2003 from $6.5 million for the first half of last year. Overall, system revenue for the first half of 2003 was $28.9 million, up $1.6 million from $27.3 million for the first half of 2002. The increase was due primarily to the second quarter of 2003 fourth arm sales. There were 28 *da Vinci* Surgical Systems shipped during the first half of 2003 compared to 29 last year.

Product sales for the three months ended June 30, 2003 of $19.2 million were up $1.0 million compared to $18.2 million for the three months ended June 30, 2002. The increase was primarily due to higher instrument and accessory sales, $1.5 million, resulting from a larger installed base of *da Vinci* Surgical Systems in 2003, offset by lower *da Vinci* Surgical System sales.

Product sales for the six months ended June 30, 2003 of $36.7 million were up $5.0 million compared to $31.7 million for the six months ended June 30, 2002. The increase was primarily due to higher instrument and accessory sales, $3.4 million, resulting from a larger installed base of *da Vinci* Surgical Systems in 2003 and additional system revenue of $1.6 million driven by incremental revenue derived from the fourth surgical arm system enhancement launched during the second quarter of 2003.

Service sales for the three months ended June 30, 2003 of $2.2 million were up $1.1 million from $1.1 million for the three months ended June 30, 2002. Service sales for the six months ended June 30, 2003 of $4.0 million were up $1.9 million from $2.1 million for the six months ended June 30, 2002. The year over year increases resulted from a larger base of *da Vinci* Surgical systems on annual service contracts.

Gross Profit. Total gross profit for the three months ended June 30, 2003 was $13.5 million, or 63.2% of sales, compared with $10.2 million, or 52.4% of sales for the three months ended June 30, 2002. The year- over-year improvement in gross profit resulted primarily from significantly lower product warranty costs resulting from system reliability improvements, improved factory productivity, and manufacturing overhead absorption timing.

Total gross profit for the six months ended June 30, 2003 was $24.0 million, or 59.1% of sales, compared with $17.1 million, or 50.5% of sales for the six months ended June 30, 2002. The year-over-year improvement in gross profit resulted primarily from significantly lower product warranty costs resulting from system reliability improvements and improved factory productivity.

Product sales gross profit percentage increased from 53.7% for the three months ended June 30, 2002 to 64.1% for the three months ended June 30, 2003. Product gross profit percentage increased from 52.2% for the six months ended June 30, 2002 to 60.0% for the six months ended June 30, 2003. The year over year increases resulted primarily from significantly lower warranty costs and improved factory productivity.

Service sales gross profit percentage increased from 31.4% for the three months ended June 30, 2002 to 55.0% for the three months ended June 30, 2003. Product gross profit percentage increased from 25.3% for the six months ended June 30, 2002 to 51.1% for the six months ended June 30, 2003. The year over year increases resulted primarily from lower per system service costs resulting from system reliability improvements and field service organization productivity gains.

Selling, General and Administrative Expenses. Selling, general and administrative expenses for the three months ended June 30, 2003 were $9.4 million, down 4% from $9.8 million for the three months ended June 30, 2002. The year-over-year decrease was primarily due to the decrease in litigation expenses of $1.4 million, offset by higher headcount and travel related costs associated with providing surgical and training support to a larger installed base of *da Vinci* Surgical Systems, a $0.5 million provision for bad debts related to accounts receivables acquired from Computer Motion and $0.1 million to record immediate expense recognition of the intangible in-process research and development acquired in the Computer Motion acquisition.

Selling, general and administrative expenses for the six months ended June 30, 2003 were $19.6 million, up 6% from $18.6 million for the six months ended June 30, 2002. The year-over-year increase was primarily due to higher headcount and travel related costs associated with supporting a larger installed base of *da Vinci* Surgical Systems of $0.9 million, bad debt expense of $0.5 million, offset by a $0.5 million insurance recovery recorded in the first quarter of 2003 related to the unauthorized purchases made in the third quarter of 2002. Please see "Part II. Item I. Legal Proceedings - Other Legal Matters."

Selling, general and administrative expenses include costs for sales, marketing and administrative personnel, tradeshow expenses, legal expenses, regulatory fees and general corporate expenses. Selling, general and administrative expenses are expected to increase in the future to support expanding business activities and integrate the Computer Motion business.

Research and Development Expenses. Research and development expenses for the three months ended June 30, 2003 were $3.6 million, down 22% from $4.6 million for the three months ended June 30, 2002. The year- over-year decrease resulted primarily from lower second quarter 2003 project materials costs of $0.6 million and lower project consulting costs of $0.4 million.

Research and development expenses for the six months ended June 30, 2003 were $7.1 million, down 21% from $8.9 million for the six months ended June 30, 2002. The year-over-year decrease resulted primarily from lower project materials costs of $0.7 million and lower project consulting costs of $0.6 million, and deferred compensation of $0.1 million. The remainder of the decrease related to lower general operating expenses.

Research and development expenses include costs associated with the design, development, testing and enhancement of our products. These enhancements represent significant improvements to our products. Research and development expenses also include expenditures for clinical trials and purchases of laboratory supplies. Research and development costs are expensed as incurred. Research and development expenses are expected to increase in the future due to the impact of the acquisition of Computer Motion.

Deferred Compensation. We record deferred compensation as the difference between the exercise price of options granted and the fair value of our common stock at the time of grant for financial reporting purposes. Deferred compensation is amortized to research and development expense and selling, general and administrative expense. Non-cash deferred compensation expense included in research and development expenses was $0.1 million and $0.1 million for the three months ended June 30, 2003 and 2002, respectively. Non- cash deferred compensation expense included in selling, general and administrative expenses was $0.1 million and $0.1 million for the three months ended June 30, 2003 and 2002, respectively. Non-cash deferred compensation expense included in research and development expenses was $0.1 million and $0.3 million for the six months ended June 30, 2003 and 2002, respectively. Non-cash deferred compensation expense included in selling, general and administrative expenses was $0.2 million and $0.1 million for the six months ended June 30, 2003 and 2002, respectively. Deferred compensation related to below market options granted prior to our initial public offering ($8.9 million) have now been fully amortized. In connection with our acquisition of Computer Motion, we recorded $0.4 million of deferred compensation on unvested options which will be amortized into compensation expense over a three year period beginning July 1, 2003 using the graded vesting method.

Other Income (Expense). Other income (expense) for the three months ended June 30, 2003 was $0.3 million, down 0.2 million compared to $0.5 million for the three months ended June 30, 2002. The decrease resulted in reduced interest earnings on lower investment balances. Other income (expense) for the six months ended June 30, 2003 was $1.2 million, up $0.2 million compared to $1.0 million for the six months ended June 30, 2002. The increase resulted primarily from $0.5 million of gains realized during the first quarter of 2003 on sales of investment securities, partially offset by reduced interest earnings on lower investment balances.

LIQUIDITY AND CAPITAL RESOURCES

Our operations have been financed through the sales of our convertible preferred stock, yielding net proceeds of approximately $127.3 million, our initial public offering of 5,750,000 shares of our common stock, yielding approximately $46.8 million, and equipment financing arrangements, yielding approximately $10.5 million. The equipment arrangements provide financing at specific interest rates for periods of up to 48 months, at which time the principal is repaid to the lessors. As collateral for the equipment financing, we have granted the lessors a security interest in equipment specified under each arrangement.

As of June 30, 2003, we had working capital of $41.6 million, compared to $52.6 million as of December 31, 2002. The decrease during the first half of 2003 resulted primarily from the impact of the acquisition of Computer Motion, reflecting cash used to fund the second quarter 2003 Computer Motion operations of $5.3 million, establishment of a restructuring accrual of $3.4 million, and the negative fair value of working capital acquired of $1.0 million. The remainder of the decrease resulted primarily from our year to date net loss of $1.4 million.

Net cash provided by operating activities for the three months ended June 30, 2003 was $2.9 million, comprised primarily of our net income of $0.9 million, non-cash expenses of $1.3 million, and working capital provided of $0.7 million. Cash provided by operating activities was $3.2 million higher in the second quarter of 2003 compared to the second quarter of 2002 primarily due to higher 2003 net income.

Net cash used by operating activities for the six months ended June 30, 2003 was $3.0 million, comprised primarily of our net loss of $1.4 million, and working capital used of $4.2 million, offset by non-cash expenses of $2.6 million. Cash used by operating activities was $4.3 million less than in the first half of 2003 compared to the first half of 2002 primarily due to lower 2003 net loss of $7.9 million, offset by working capital used of $3.9 million.

Net cash used by investing activities was $7.7 million for the three months ended June 30, 2003, compared to $16.7 million provided for the three months ended June 30, 2002. Second quarter 2003 cash used in investing activities consisted of $4.1 million of net cash used to fund the operations of Computer Motion, $2.9 million to purchase short-term investments, and $0.7 million invested in property and equipment. Second quarter 2002 cash provided by investing activities consisted of $17.5 million of proceeds from sales and maturities of investments, offset by investments in property and equipment of $0.8 million.

Net cash provided by investing activities for the six months ended June 30, 2003 of $2.5 million was $17.6 million less than $20.1 million for the six months ended June 30, 2002 primarily due to lower net movement into cash from short-term investments of $17.2 million resulting from lower 2003 first half net loss and general timing of conversions into cash to support short-term liquidity.

Net cash used by financing activities was $0.2 million for the three months ended June 30, 2003, compared to $0.8 million for the three months ended June 30, 2002. This decrease resulted from lower long-term borrowing net proceeds of $0.4 million, offset by higher proceeds from issuance of common stock of $0.2 million. Net cash provided by financing activities was $0.8 million for the six months ended June 30, 2003, compared to $0.7 million for the six months ended June 30, 2002. This decrease resulted from higher proceeds from issuance of common stock of $0.5 million, offset by lower long- term borrowing net proceeds.

We believe the Company has sufficient cash to complete the Computer Motion integration and reach sustained cash-positive operations. We ended our second quarter 2003 with $42.9 in total cash, cash equivalents, and short-term investments. Based upon our current business forecast and our restructuring plan, we expect year-end 2003 cash, cash equivalents, and short- term investments to total approximately $25.0 million by which time we expect to have substantially completed our integration activities, incurred most of our integration costs, and achieve cash positive operations. Our ability to achieve these goals is subject to economic conditions and unanticipated changes in business conditions, and therefore there can be no assurance that these results will be achieved.

Our capital requirements depend on numerous factors, including the effects of our recently completed merger with Computer Motion, market acceptance of our products, the resources we devote to developing and supporting our products, and other factors. We expect to devote substantial capital resources to continue our research and development efforts, to expand our support and product development activities and for other general corporate activities. We believe that our current cash and short- term investment balances, together with revenue to be derived from the sale of our products, will be sufficient to fund our future operations. However, if cash generated by operations is insufficient to satisfy our liquidity requirements, we may need to sell additional equity or debt securities or obtain additional credit arrangements. Additional financing may not be available on terms acceptable to us or at all. The sale of additional equity or convertible debt securities may result in additional dilution to our stockholders.

Contractual Obligations and Commercial Commitments

The following table summarizes all significant contractual payment obligations by payment due date:

Payments by Periods (Millions)

Contractual Obligation	Total	Under 1 Year	1-3 Years	3-5 Years	Over 5 Years
Long-term debt	$ 2.6	$ 1.4	$ 1.2	$ -	$ -
Building lease	14.1	3.5	10.5	.1	-
Total	$ 16.7	$ 4.9	$ 11.7	$ .1	$ -

CRITICAL ACCOUNTING POLICIES

We believe the following represent our critical accounting policies:

Revenue Recognition. In certain cases, revenue from direct system sales is generated from multiple-element arrangements which require judgment in the areas of customer acceptance, training, installation and collectibility. The Company accounts for multiple-element arrangements in accordance with the provisions of SAB 101, "Revenue Recognition in Financial Statements." Revenue is recognized as specific elements indicated in sales contracts are executed. If an element is essential to the functionality of an arrangement, the entire arrangement's revenue is deferred until that essential element is delivered. The fair value of each undelivered element that is not essential to the functionality of the system is deferred until performance or delivery occurs. The fair value of an undelivered

element is based upon an estimate made by management. If an undelivered element exists, the Company will determine the fair value of the undelivered element and subtract the fair value of the undelivered element from the total consideration under the arrangement. The residual amount is recognized as the value of the delivered element. Amounts billed in excess of revenue recognized are recorded as deferred revenue on the balance sheet. Costs associated with inconsequential or perfunctory elements in multiple-element arrangements are accrued at the time revenue is recognized. The Company accounts for installation as a separate element of a multiple-element arrangement. The Company therefore recognizes the fair value of the installation services upon completion of installation.

Revenue from sales of instruments and accessories is recognized upon shipment. Revenue related to future commitments under service contracts is deferred and recognized ratably over the service period. All costs associated with the provision of service and maintenance, including salaries, benefits, travel, spare parts and equipment, are recognized in cost of sales as incurred. Amounts billed in excess of revenue recognized are included as deferred revenue in the accompanying consolidated balance sheets.

Allowance for Doubtful Accounts. The allowance for doubtful accounts is based upon management estimates. Factors underlying these estimates include analysis of days outstanding, customer payment history and management judgment. The allowance is adjusted periodically to reflect current data, activity, and associated risks.

Inventory Reserves. We write our inventory down for estimated obsolescence or unmarketable inventory equal to the difference between the cost of inventory and the estimated market value based upon assumptions about future demand and market conditions. If actual future demand or market conditions are less favorable than those projected by management, additional inventory write- downs may be required in the future.

Intangible Assets. We have intangible assets on our balance sheet related to the acquisition of Computer Motion and the acquisition of other patents. The valuation and classification of these assets and the assignment of useful amortization lives involves judgments and the use of estimates. The evaluation of these intangibles for impairment under established accounting guidelines is required on an ongoing basis. Changes in business conditions could potentially require future adjustments to asset valuations.

Goodwill. We have goodwill on our balance sheet relating to the acquisition of Computer Motion. Goodwill is recorded as the excess of the purchase price over the fair value of the net tangible and intangible assets acquired. Goodwill is not amortized, rather is tested for impairment at lease annually. In the event we determine that goodwill has been impaired, we will record an accounting charge for the impairment during the fiscal quarter in which the determination is made.

Warranties. We provide for the estimated costs of product warranties at the time revenue is recognized. Our estimate of costs to service our warranty obligations is based upon historical experience and expectation of future conditions. If warranty claim activity and the costs associated with servicing those claims differ from our estimates, revisions to the estimated warranty liability may be required.

Contingencies. We are subject to proceedings, lawsuits and other claims related to our products, patents and other matters. We are required to assess the likelihood of any adverse judgments or outcomes to these matters as well as potential ranges of probable losses. A determination of the amount of reserves required, if any, for these contingencies is made after careful analysis of each individual issue. The required reserves may change in the future due to new developments in each matter or changes in approach such as a change in settlement strategy in dealing with these matters.

FACTORS AFFECTING OPERATING RESULTS

OUR FUTURE OPERATING RESULTS MAY BE BELOW SECURITIES ANALYSTS' OR INVESTORS' EXPECTATIONS, WHICH COULD CAUSE OUR STOCK PRICE TO DECLINE.

Because of our limited operating history, we have limited insight into trends that may emerge in our market and affect our business. The revenue and income potential of our market are unproven, and we may be unable to generate significant revenues. In addition, our costs may be higher than we, securities analysts or investors expect. If we fail to generate sufficient revenues or our costs are higher than we expect, our results of operations will suffer, which in turn could cause our stock price to decline. Further, future revenue from sales of our products is difficult to forecast because the market for new surgical technologies is still evolving. Our results of operations will depend upon numerous factors, including:

- the progress and results of clinical trials;
- actions relating to regulatory matters;
- the integration of Computer Motion with our company;
- the extent to which our products gain market acceptance;
- our timing and ability to develop our manufacturing and sales and marketing capabilities;
- demand for our products;
- the progress of surgical training in the use of our products;
- our ability to develop, introduce and market new or enhanced versions of our products on a timely basis;
- product quality problems;
- our ability to protect our proprietary rights and defend against third party challenges;
- our ability to license additional intellectual property rights; and
- third-party payor reimbursement policies.

Our operating results in any particular period will not be a reliable indication of our future performance. It is likely that in some future quarters, our operating results will be below the expectations of securities analysts or investors. If this occurs, the price of our common stock, and the value of your investment, will likely decline.

WE EXPERIENCE LONG AND VARIABLE SALES CYCLES, WHICH COULD HAVE A NEGATIVE IMPACT ON OUR RESULTS OF OPERATIONS FOR ANY GIVEN QUARTER.

Our *da Vinci* Surgical System has a lengthy sales and purchase order cycle because it is a major capital item and generally requires the approval of senior management at purchasing institutions. These factors may contribute to substantial fluctuations in our quarterly operating results, particularly during the periods in which our sales volume is low. Because of these fluctuations, it is likely that in some future quarters our operating results will fall below the expectations of securities analysts or investors. If that happens, the market price of our stock would likely decrease. These fluctuations also mean that you will not be able to rely upon our operating results in any particular period as an indication of future performance.

BECAUSE A SMALL NUMBER OF CUSTOMERS HAVE AND ARE LIKELY TO CONTINUE TO ACCOUNT FOR A SUBSTANTIAL PORTION OF OUR REVENUES, OUR REVENUES COULD DECLINE DUE TO THE LOSS OR DELAY OF A SINGLE CUSTOMER.

A relatively small number of customers account for a significant portion of our total revenues. During the three months ended June 30, 2003 and 2002, approximately 70% and 80%, respectively, of our revenues came from the sales of *da Vinci* Surgical Systems, which are high revenue dollar items. During the six

months ended June 30, 2003 and 2002, approximately 71% and 81%, respectively, of our revenues came from the sales of *da Vinci* Surgical Systems During the three and six month periods ended June 30, 2003 and 2002, no customer accounted for more than 10% of total sales. However, due to the high average selling price of the *da Vinci* Surgical System, our failure to add new customers that make significant purchases of our products could reduce our future revenues. The loss or delay of individual orders could have a significant impact on revenues and operating results.

IF OUR PRODUCTS DO NOT ACHIEVE MARKET ACCEPTANCE, WE WILL NOT BE ABLE TO GENERATE THE REVENUE NECESSARY TO SUPPORT OUR BUSINESS.

Our products represent a fundamentally new way of performing surgery. Achieving physician, patient and third-party payor acceptance of *Intuitive* surgery as a preferred method of performing surgery will be crucial to our success. If our products fail to achieve market acceptance, hospitals will not purchase our products and we will not be able to generate the revenue necessary to support our business. We believe that physicians' and third-party payors' acceptance of the benefits of procedures performed using our products will be essential for acceptance of our products by patients. Physicians will not recommend the use of our products unless we can demonstrate that they produce results comparable or superior to existing surgical techniques. Even if we can prove the effectiveness of our products through clinical trials, surgeons may elect not to use our products for any number of other reasons. For example, cardiologists may continue to recommend conventional open-heart surgery simply because such surgery is already widely accepted. In addition, surgeons may be slow to adopt our products because of the perceived liability risks arising from the use of new products and the uncertainty of reimbursement from third-party payors.

We expect that there will be a learning process involved for surgical teams to become proficient in the use of our products. Broad use of our products will require training of surgical teams. Market acceptance could be delayed by the time required to complete this training. We may not be able to rapidly train surgical teams in numbers sufficient to generate adequate demand for our products. We cannot be certain that our training programs will be cost effective or sufficient to meet our customers' needs.

WE ARE INVOLVED IN INTELLECTUAL PROPERTY LITIGATION WITH BROOKHILL-WILK 1, LLC THAT MAY HURT OUR COMPETITIVE POSITION, MAY BE COSTLY TO US AND MAY PREVENT US FROM SELLING OUR PRODUCTS.

On September 1, 2000 Brookhill-Wilk 1, LLC ("Wilk") filed a lawsuit against Intuitive Surgical in the United States District Court for the Southern District of New York (Case No. 00 Civ. 6599 (NRB)) alleging that by making, using, selling or offering for sale our *da Vinci* Surgical System, we are infringing U.S. Patent Nos. 5,217,003 and 5,368,015 in willful disregard of Wilk's patent rights. These patents concern methods and devices for "remote" surgery. In March 2001, Wilk withdrew its assertion of the '015 patent against our company. On November 8, 2001, in response to a motion on one of Intuitive Surgical's noninfringement defenses, the District Court granted summary judgment of noninfringement of the '003 patent in our favor and dismissed Wilk's complaint in its entirety without prejudice. Wilk appealed the summary judgment ruling to the U.S. Court of Appeals for the Federal Circuit.

On April 11, 2003, the Court of Appeals reversed the District Court's judgment and remanded the case for further proceedings. This reversal is based on the Court of Appeals' determination that the particular claim limitation at issue should be interpreted differently than as construed by the District Court. The Court of Appeals has since clarified its opinion in response to Intuitive Surgical's petition for rehearing. Upon remand, we intend to continue to vigorously defend our rights and, if necessary, are prepared to continue to dispute the meaning of other portions of the asserted claim language and to conduct discovery and file further motions on whether the patent is infringed, valid and/or enforceable. We believe that we will prevail in the litigation and that we have multiple meritorious defenses to Wilk's allegations. However, litigation is unpredictable and we may not prevail. The case remains in its early stages of discovery in the District Court.

If we lose Wilk's suit against us, it will hurt our competitive position, may be costly to us and may prevent us from selling our products. If we lose the patent suit, we may need to obtain from Wilk a license to this technology if we are to continue to market our products that have been found to infringe Wilk's patents. This license could be expensive, which could seriously harm our business. If Wilk is successful in its suit against us and is unwilling to grant us a license, we may be required to stop selling our products that are found to infringe Wilk's patents unless we can redesign them so they do not infringe Wilk's patents, which we may be unable to do. In addition, we could be required to pay Wilk damages, including treble damages, which could be substantial and harm our financial position. Due to the inherent uncertainties of litigation, however, the Company cannot accurately predict the ultimate outcome of the litigation against Wilk at this time and, therefore, cannot estimate the range of possible loss.

The foregoing proceeding could be expensive to litigate, may be protracted and our confidential information may be compromised. Whether or not we are successful in this lawsuit, the proceeding could consume substantial amounts of our financial and managerial resources. At any time, Wilk may file additional claims against our company, or we may file claims against Wilk, which could increase the risk, expense and duration of the litigations. For more information on our litigation with Wilk, see "Part II-Item 1: Legal Proceedings."

IF WE ARE UNABLE TO PROTECT THE INTELLECTUAL PROPERTY CONTAINED IN OUR PRODUCTS FROM USE BY THIRD PARTIES, OUR ABILITY TO COMPETE IN THE MARKET WILL BE HARMED.

Our commercial success will depend in part on obtaining patent and other intellectual property protection for the technologies contained in our products, and on successfully defending our patents and other intellectual property against third party challenges.

We will incur substantial costs in obtaining patents and, if necessary, defending our proprietary rights. The patent positions of medical device companies, including ours, can be highly uncertain and involve complex and evolving legal and factual questions. We do not know whether we will obtain the patent protection we seek, or that the protection we do obtain will be found valid and enforceable if challenged. We also do not know whether we will be able to develop additional patentable proprietary technologies. If we fail to obtain adequate protection of our intellectual property, or if any protection we obtain is reduced or eliminated, others could use our intellectual property without compensating us, resulting in harm to our business. We may also determine that it is in our best interests to voluntarily challenge a third party's products or patents in litigation or administrative proceedings, including patent interferences or reexaminations. In addition, the laws of certain foreign countries do not protect intellectual property rights to the same extent as do the laws of the United States.

OTHERS MAY ASSERT THAT OUR PRODUCTS INFRINGE THEIR INTELLECTUAL PROPERTY RIGHTS, WHICH MAY CAUSE US TO ENGAGE IN COSTLY DISPUTES AND, IF WE ARE NOT SUCCESSFUL IN DEFENDING OURSELVES, COULD ALSO CAUSE US TO PAY SUBSTANTIAL DAMAGES AND PROHIBIT US FROM SELLING OUR PRODUCTS.

We are aware of both United States and foreign patents issued to third parties that relate to computer-assisted surgery, remote surgery, and minimally invasive surgery. Some of these patents on their face appear broad enough to cover one or more aspects of our present technology, and may cover aspects of our future technology. We do not know whether any of these patents, if challenged, would be held valid, enforceable and infringed. From time to time, we receive, and likely will continue to receive, letters from third parties inviting us to license their patents. We may be sued by, or become involved in an administrative proceeding with, one or more of these third parties. We cannot assure you that a court or administrative body would agree with any arguments or defenses we have concerning invalidity, unenforceability or noninfringement of any third-party patent. In addition to the issued patents of which we are aware, other parties may have filed, and in the future are likely to file, patent applications covering surgical products that are similar or identical to ours. We cannot assure you that any patents issuing from applications filed by a third party will not cover our products or will not have priority over our patent applications.

The medical device industry has been characterized by extensive litigation and administrative proceedings regarding patents and other intellectual property rights, and companies have employed such actions to gain a competitive advantage. If third parties assert infringement or other intellectual property claims against us as Brookhill-Wilk 1, LLC has, our technical and management personnel will experience a significant diversion of time and effort and we will incur large expenses defending our company. If third parties in any patent action are successful, our patent portfolio may be damaged, we may have to pay substantial damages, including treble damages, and we may be required to stop selling our products or obtain a license which, if available at all, may require us to pay substantial royalties. We cannot be certain that we will have the financial resources or the substantive arguments to defend our patents from infringement or claims of invalidity or unenforceability, or to defend against allegations of infringement of third- party patents. In addition, any public announcements related to litigation or administrative proceedings initiated by us, or initiated or threatened against us, could cause our stock price to decline.

THE RIGHTS AND MEASURES WE RELY ON TO PROTECT THE INTELLECTUAL PROPERTY UNDERLYING OUR PRODUCTS MAY NOT BE ADEQUATE TO PREVENT THIRD PARTIES FROM USING OUR TECHNOLOGY WHICH COULD HARM OUR ABILITY TO COMPETE IN THE MARKET.

In addition to patents, we typically rely on a combination of trade secret, copyright and trademark laws, nondisclosure agreements and other contractual provisions and technical security measures to protect our intellectual property rights. Nevertheless, these measures may not be adequate to safeguard the technology underlying our products. If they do not protect our rights adequately, third parties could use our technology, and our ability to compete in the market would be reduced. In addition, employees, consultants and others who participate in developing our products may breach their agreements with us regarding our intellectual property, and we may not have adequate remedies for the breach. We also may not be able to effectively protect our intellectual property rights in some foreign countries. For a variety of reasons, we may decide not to file for patent, copyright or trademark protection outside the United States. We also realize that our trade secrets may become known through other means not currently foreseen by us. Notwithstanding our efforts to protect our intellectual property, our competitors may independently develop similar or alternative technologies or products that are equal or superior to our technology and products without infringing any of our intellectual property rights, or may design around our proprietary technologies. For further information on our intellectual property and the difficulties in protecting it, see "Item 1: Business -- Intellectual Property," included in the Annual Report on Form 10-K/A of Intuitive Surgical, Inc., filed with the SEC.

OUR PRODUCTS RELY ON LICENSES FROM THIRD PARTIES, AND IF WE LOSE ACCESS TO THESE TECHNOLOGIES, OUR REVENUES COULD DECLINE.

We rely on technology that we license from others, including technology that is integral to our products. We have entered into license agreements with SRI International, IBM Corporation, MIT, Olympus Optical Co., Ltd., and Heartport, Inc.,now part of Johnson & Johnson. Any of these agreements may be terminated for breach. If any of these agreements is terminated, we may be unable to reacquire the necessary license on satisfactory terms, or at all. The loss or failure to maintain these licenses could prevent or delay further development or commercialization of our products. See "Item 1: Business -- Intellectual Property," included in the Annual Report on Form 10-K/A of Intuitive Surgical, Inc., filed with the SEC.

PUBLIC ANNOUNCEMENTS OF LITIGATION EVENTS MAY CAUSE OUR STOCK PRICE TO DECLINE.

During the course of our administrative proceedings and/or lawsuits, there may be public announcements of the results of hearings, motions, and other interim proceedings or developments in the litigation. If securities analysts or investors perceive these results to be negative, it could have a substantial negative effect on the trading price of our stock.

OUR PRODUCTS ARE SUBJECT TO A LENGTHY AND UNCERTAIN DOMESTIC REGULATORY PROCESS. IF WE DO NOT OBTAIN AND MAINTAIN THE NECESSARY DOMESTIC REGULATORY APPROVALS, WE WILL NOT BE ABLE TO MARKET AND SELL OUR PRODUCTS IN THE UNITED STATES.

Our products and operations are subject to extensive regulation in the United States by the U.S. Food and Drug Administration, or FDA. The FDA regulates the research, testing, manufacturing, safety, labeling, storage, recordkeeping, promotion, distribution and production of medical devices in the United States to ensure that medical products distributed domestically are safe and effective for their intended uses. In order for us to market certain products for use in the United States, we generally must first obtain clearance from the FDA pursuant to Section 510(k) of the Federal Food, Drug, and Cosmetic Act, or FFDCA. Clearance under Section 510(k) requires demonstration that a new device is substantially equivalent to another legally marketed device. If we modify our products after they receive FDA clearance, the FDA may require us to submit a separate 510(k) or premarket approval application, or PMA, for the modified product before we are permitted to market the products in the U.S. In addition, if we develop products in the future that are not considered to be substantially equivalent to a legally marketed device, we will be required to obtain FDA approval by submitting a PMA.

The FDA may not act favorably or quickly in its review of our 510(k) or PMA submissions, or we may encounter significant difficulties and costs in our efforts to obtain FDA clearance or approval, all of which could delay or preclude sale of new products in the United States. Furthermore, the FDA may request additional data or require us to conduct further testing, or compile more data, including clinical data and clinical studies, in support of a 510(k) submission. The FDA may also, instead of accepting a 510(k) submission, require us to submit a PMA, which is typically a much more complex application than a 510(k). To support a PMA, the FDA would likely require that we conduct one or more clinical studies to demonstrate that the device is safe and effective, rather than substantially equivalent to another legally marketed device. We may not be able to meet the requirements to obtain 510(k) clearance or PMA approval, or the FDA may not grant any necessary clearances or approvals. In addition, the FDA may place significant limitations upon the intended use of our products as a condition to a 510(k) clearance or PMA approval. Product applications can also be denied or withdrawn due to failure to comply with regulatory requirements or the occurrence of unforeseen problems following clearance or approval. Any delays or failure to obtain FDA clearance or approvals of new products we develop, any limitations imposed by the FDA on new product use, or the costs of obtaining FDA clearance or approvals could have a material adverse effect on our business, financial condition and results of operations.

In order to conduct a clinical investigation involving human subjects for the purpose of demonstrating the safety and effectiveness of a device, a company must, among other things, apply for and obtain Institutional Review Board, or IRB approval of the proposed investigation. In addition, if the clinical study involves a "significant risk" (as defined by the FDA) to human health, the sponsor of the investigation must also submit and obtain FDA approval of an investigational device exemption, or IDE application. We may not be able to obtain FDA and/or IRB approval to undertake clinical trials in the U.S. for any new devices we intend to market in the United States in the future. If we obtain such approvals, we may not be able to comply with the IDE and other regulations governing clinical investigations or the data from any such trials may not support clearance or approval of the investigational device. Failure to obtain such approvals or to comply with such regulations could have a material adverse effect on our business, financial condition and results of operations. For additional information concerning regulatory approvals of our products, see "Item 1: Business -- Government Regulation," included in the Annual Report on Form 10-K/A of Intuitive Surgical, Inc., filed with the SEC.

OUR PRODUCTS ARE SUBJECT TO VARIOUS INTERNATIONAL REGULATORY PROCESSES AND APPROVAL REQUIREMENTS. IF WE DO NOT OBTAIN AND MAINTAIN THE NECESSARY INTERNATIONAL REGULATORY APPROVALS, WE WILL NOT BE ABLE TO MARKET AND SELL OUR PRODUCTS IN FOREIGN COUNTRIES.

To be able to market and sell our products in other countries, we must obtain regulatory approvals and comply with the regulations of those countries. These regulations, including the requirements for approvals, and the time required for regulatory review vary from country to country. Obtaining and maintaining foreign regulatory approvals are expensive, and we cannot be certain that we will receive regulatory approvals in any foreign country in which we plan to market our products. If we fail to obtain regulatory approval in any foreign country in which we plan to market our products, our ability to generate revenue will be harmed.

The European Union requires that manufacturers of medical products obtain the right to affix the CE mark to their products before selling them in member countries of the European Union. The CE mark is an international symbol of adherence to quality assurance standards and compliance with applicable European medical device directives. In order to obtain the right to affix the CE mark to products, a manufacturer must obtain certification that its processes meet certain European quality standards. In January 1999, we received permission to affix the CE mark to our *da Vinci* Surgical System and *EndoWrist* instruments.

If we modify existing products or develop new products in the future, including new instruments, we may need to apply for permission to affix the CE mark to such products. In addition, we will be subject to annual regulatory audits in order to maintain the CE mark permissions we have already obtained. We cannot be certain that we will be able to obtain permission to affix the CE mark for new or modified products or that we will continue to meet the quality and safety standards required to maintain the permissions we have already received. If we are unable to maintain permission to affix the CE mark to our products, we will no longer be able to sell our products in member countries of the European Union. For additional information concerning regulatory approvals of our products, see "Item 1: Business -- Government Regulation," included in the Annual Report on Form 10-K/A of Intuitive Surgical, Inc., filed with the SEC.

IF INSTITUTIONS OR SURGEONS ARE UNABLE TO OBTAIN REIMBURSEMENT FROM THIRD- PARTY PAYORS FOR PROCEDURES USING OUR PRODUCTS, OR IF REIMBURSEMENT IS INSUFFICIENT TO COVER THE COSTS OF PURCHASING OUR PRODUCTS, WE MAY BE UNABLE TO GENERATE SUFFICIENT SALES TO SUPPORT OUR BUSINESS.

Domestic institutions will typically bill the services performed with our products to various third-party payors, such as Medicare, Medicaid and other government programs and private insurance plans. If hospitals do not obtain sufficient reimbursement from third-party payors for procedures performed with our products, or if government and private payors' policies do not permit reimbursement for surgical procedures performed using our products, we may not be able to generate the revenues necessary to support our business. Our success in international markets also depends upon the eligibility of our products for reimbursement through government-sponsored health care payment systems and third-party payors. Reimbursement practices vary significantly by country. Many international markets have government-managed healthcare systems that control reimbursement for new products and procedures. Other foreign markets have both private insurance systems and government-managed systems that control reimbursement for new products and procedures. Market acceptance of our products may depend on the availability and level of reimbursement in any country within a particular time. In addition, health care cost containment efforts similar to those we face in the United States are prevalent in many of the other countries in which we intend to sell our products and these efforts are expected to continue. For further information on third-party reimbursement policies, see "Item 1: Business -- Third-Party Reimbursement," included in the Annual Report on Form 10-K/A of Intuitive Surgical, Inc., filed with the SEC.

BECAUSE OUR MARKETS ARE HIGHLY COMPETITIVE, CUSTOMERS MAY CHOOSE TO PURCHASE OUR COMPETITORS' PRODUCTS OR MAY NOT ACCEPT INTUITIVE SURGERY, WHICH WOULD RESULT IN REDUCED REVENUE AND LOSS OF MARKET SHARE.

Intuitive surgery is a new technology that must compete with established minimally invasive surgery and open surgery. These procedures are widely accepted in the medical community and in many cases have a long history of use. We also face competition from several companies that are developing new approaches and products for the minimally invasive surgery market. In addition, we presently face increasing competition from companies who are developing robotic and computer-assisted surgical systems. Our revenues may be reduced or eliminated if our competitors develop and market products that are more effective or less expensive than our products. If we are unable to compete successfully, our revenues will suffer. We may not be able to maintain or improve our competitive position against current or potential competitors, especially those with greater resources.

In many cases, the medical conditions that can be treated using our products can also be treated by drugs or other medical devices and procedures. Many of these alternative treatments are also widely accepted in the medical community and have a long history of use. In addition, technological advances could make such treatments more effective or less expensive than using our products, which could render our products obsolete or unmarketable. We cannot be certain that physicians will use our products to replace or supplement established treatments or that our products will be competitive with current or future technologies.

IF DEFECTS ARE DISCOVERED IN OUR PRODUCTS, WE MAY INCUR ADDITIONAL UNFORESEEN COSTS, HOSPITALS MAY NOT PURCHASE OUR PRODUCTS AND OUR REPUTATION MAY SUFFER.

Our products incorporate mechanical parts and computer software, either of which can contain errors or failures, especially when first introduced. In addition, new products or enhancements may contain undetected errors or performance problems that, despite testing, are discovered only after commercial shipment. Because our products are designed to be used to perform complex surgical procedures, we expect that our customers will have an increased sensitivity to such defects. We cannot assure you that our products will not experience errors or performance problems in the future. If we experience flaws or performance problems, any of the following could occur:

- delays in product shipments;
- loss of revenue;
- delay in market acceptance;
- diversion of our resources;
- damage to our reputation;
- increased service or warranty costs; or
- product liability claims.

WE HAVE LIMITED EXPERIENCE IN MANUFACTURING OUR PRODUCTS AND MAY ENCOUNTER MANUFACTURING PROBLEMS OR DELAYS THAT COULD RESULT IN LOST REVENUE.

We have manufactured a limited number of our products for sales to customers. We may be unable to establish or maintain reliable, high- volume manufacturing capacity. Even if this capacity can be established and maintained, the cost of doing so may increase the cost of our products and reduce our ability to compete. We may encounter difficulties in scaling up production of our products, including:

- problems involving production yields;
- quality control and assurance;
- component supply shortages;
- shortages of qualified personnel; and
- compliance with state, federal and foreign regulations.

Manufacturing our products is a complex process. If demand for our products exceeds our manufacturing capacity, we could develop a substantial backlog of customer orders. If we are unable to establish and maintain larger-scale manufacturing capabilities, our ability to generate revenues will be limited and our reputation in the marketplace would be damaged.

IF OUR MANUFACTURING FACILITIES DO NOT CONTINUE TO MEET FEDERAL, STATE OR EUROPEAN MANUFACTURING STANDARDS, WE MAY BE REQUIRED TO TEMPORARILY CEASE ALL OR PART OF OUR MANUFACTURING OPERATIONS, WHICH WOULD RESULT IN PRODUCT DELIVERY DELAYS AND LOST REVENUE.

Our manufacturing facilities are subject to periodic inspection by regulatory authorities and our operations will continue to be regulated by the FDA for compliance with Good Manufacturing Practice requirements contained in the FDA's Quality System Regulations, or QSR. We are also required to comply with International Organization for Standardization, or ISO quality system standards in order to produce products for sale in Europe. If we fail to continue to comply with Good Manufacturing Practice requirements or ISO standards, we may be required to cease all or part of our operations until we comply with these regulations. We are currently in compliance with ISO standards. The FDA inspected our Mountain View and Sunnyvale facilities in March 2000 and December 2002, respectively. The Good Manufacturing Practice issues raised by the FDA during the inspections either were satisfactorily resolved with the FDA, or we believe can be resolved by us to the FDA's satisfaction, although we cannot assure you that we will be able to do so. We continue to be subject to FDA inspections at any time. Maintaining such compliance is difficult and costly. We cannot be certain that our facilities will be found to comply with Good Manufacturing Practice requirements or ISO standards in future inspections and audits by regulatory authorities.

The state of California also requires that we maintain a license to manufacture medical devices. Our facilities and manufacturing processes were inspected in February 1998. In March 1998, we passed the inspection and received a device manufacturing license from the California Department of Health Services. In March 2002, our facilities and manufacturing processes in our Sunnyvale facility were re-inspected by the Food and Drug Branch, or FDB, and we were issued an updated device manufacturing license for our Sunnyvale facility. We are subject to periodic inspections by the California Department of Health Services and if we are unable to maintain this license following any future inspections, we will be unable to manufacture or ship any products.

OUR RELIANCE ON SOLE AND SINGLE SOURCE SUPPLIERS COULD HARM OUR ABILITY TO MEET DEMAND FOR OUR PRODUCTS IN A TIMELY MANNER OR WITHIN BUDGET.

Some of the components necessary for the assembly of our products are currently provided to us by sole source suppliers or single source suppliers. We purchase components through purchase orders rather than long-term supply agreements and generally do not maintain large volumes of inventory. The disruption or termination of the supply of components could cause a significant increase in the costs of these components, which could affect our profitability. A disruption or termination in the supply of components could also result in our inability to meet demand for our products, which could harm our ability to generate revenues, lead to customer dissatisfaction and damage our reputation. Furthermore, if we are required to change the manufacturer of a key component of our products, we may be required to verify that the new manufacturer maintains facilities and procedures that comply with quality standards and with all applicable regulations and guidelines. The delays associated with the verification of a new manufacturer could delay our ability to manufacture our products in a timely manner or within budget.

THE USE OF OUR PRODUCTS COULD RESULT IN PRODUCT LIABILITY CLAIMS THAT COULD BE EXPENSIVE, DIVERT MANAGEMENT'S ATTENTION AND HARM OUR BUSINESS.

Our business exposes us to significant risks of product liability claims. The medical device industry has historically been litigious, and we face financial exposure to product liability claims if the use of our products were to cause injury or death. There is also the possibility that defects in the design or manufacture of our products might necessitate a product recall. Although we maintain product liability insurance, the coverage limits of these policies may not be adequate to cover future claims. Particularly as sales of our products increase, we may be unable to maintain product liability insurance in the future at satisfactory rates or in adequate amounts. A product liability claim, regardless of its merit or eventual outcome, could result in significant legal defense costs. A product liability claim or any product recalls could also harm our reputation or result in a decline in revenues.

During the second quarter 2003, two former patients of The Valley Hospital in New Jersey filed suit against The Valley Hospital, their surgeon(s) and Intuitive Surgical, Inc. alleging various harms caused during their earlier surgeries. Intuitive was named because the *da Vinci* System was utilized for a portion of the complained-of surgeries and a small portion of the tip of an *EndoWrist* instrument remained in each patient after each surgery. Each suit presents multiple claims variously alleging, among others, negligence, carelessness and/or recklessness by each defendant, that the *da Vinci* System was defectively designed and manufactured, that Intuitive failed to properly instruct and train its surgeon in its use, and that the defendants failed to properly apprise the patients of the risks involved. Each suit seeks an unspecified amount of general, special and punitive damages from the defendants, in addition to a request to recover the costs of suit and attorney fees. As each suit was just recently filed, both are in very early stages and discovery has not yet begun.

IF WE LOSE OUR KEY PERSONNEL OR ARE UNABLE TO ATTRACT AND RETAIN ADDITIONAL PERSONNEL, OUR ABILITY TO COMPETE WILL BE HARMED.

We are highly dependent on the principal members of our management and scientific staff. Our product development plans depend in part on our ability to attract and retain engineers with experience in mechanics, software and optics. Attracting and retaining qualified personnel will be critical to our success, and competition for qualified personnel is intense. We may not be able to attract and retain personnel on acceptable terms given the competition for such personnel among technology and healthcare companies, and universities. The loss of any of these persons or our inability to attract and retain qualified personnel could harm our business and our ability to compete.

INTERNATIONAL SALES OF OUR PRODUCTS ACCOUNT FOR A SIGNIFICANT PORTION OF OUR REVENUES, WHICH EXPOSES US TO RISKS INHERENT IN INTERNATIONAL OPERATIONS. OUR GROWTH MAY BE LIMITED IF WE ARE UNABLE TO SUCCESSFULLY MANAGE OUR INTERNATIONAL ACTIVITIES.

Our business currently depends in large part on our activities in Europe and other foreign markets. Sales to markets outside of the United States accounted for approximately 30% of our sales for the three months ended June 30, 2003 and 20% for the three months ended June 30, 2002. Sales to markets outside of the United States accounted for approximately 24% of our sales for the six months ended June 30, 2003 and 17% for the six months ended June 30, 2002.

We are subject to a number of challenges that specifically relate to our international business activities. These challenges include:

- failure of local laws to provide the same degree of protection against infringement of our intellectual property;
- protectionist laws and business practices that favor local competitors, which could slow our growth in international markets;
- the risks associated with foreign currency exchange rate fluctuation;
- the expense of establishing facilities and operations in new foreign markets; and
- building an organization capable of supporting geographically dispersed operations.

Currently, a majority of our international sales are denominated in U.S. dollars. As a result, an increase in the value of the U.S. dollar relative to foreign currencies could make our products less competitive in international markets. If we are unable to meet and overcome these challenges, our international operations may not be successful, which would limit the growth of our business.

RISK FACTORS ASSOCIATED WITH OUR MERGER WITH COMPUTER MOTION

INTUITIVE SURGICAL AND COMPUTER MOTION EACH HAVE INCURRED SUBSTANTIAL LOSSES SINCE INCEPTION. THE MERGED COMPANY MAY NOT BE ABLE TO GENERATE OR RAISE SUFFICIENT CASH TO FUND OPERATIONS.

For the three months ended June 30, 2003 on a stand alone basis, we generated our first net profit of $0.9 million, while Computer Motions incurred a net loss of $5.9 million, including the benefit of a $4.4 million recovery of a litigation judgment accrual with Intuitive originally charged to expense in 2002. On a year-to date basis, Intuitive Surgical incurred a $1.4 million loss and Computer Motion incurred a net loss of $13.6 million, including the litigation judgment recovery. In addition, the integration of the two companies and the settlement of outstanding Computer Motion liabilities and commitments will require significant cash resources. While we expect that we have enough cash to integrate the companies and achieve profitable operations, the extent of our future losses and the timing of achieving profitability on a merged basis are highly uncertain, and we may never achieve profitable operations. If achieving profitable operations takes longer than planned, we will need to raise additional funds. We may not be able to obtain additional financing on favorable terms, or at all. If we are unable to generate sufficient capital to fund our operations and cannot raise it on acceptable terms, we may not be able to further develop, enhance or expand the market for our products and service, and the combined company could fail.

THE COMBINED COMPANY MAY NOT REALIZE ALL OF THE ANTICIPATED BENEFITS OF THE MERGER.

The success of the merger will depend, in part, on the ability of the combined company to realize the anticipated synergies, cost savings and growth opportunities from integrating the business of Computer Motion with the business of Intuitive Surgical. Our success in realizing these benefits and the timing of this realization depend upon the successful, rapid integration of the operations of Computer Motion with those of Intuitive Surgical. This integration will be a complex, costly and time-consuming process, and may not succeed as planned. The difficulties of combining the operations of the companies include, among other things:

- coordinating and consolidating ongoing and future research and development efforts;
- consolidating sales and marketing operations;
- retaining existing customers and attracting new customers;
- retaining strategic partners and attracting new strategic partners;
- retaining key employees;
- consolidating corporate and administrative infrastructures;
- integrating and managing the technologies and products of the two companies;
- identifying and eliminating redundant and underperforming operations and assets;
- using capital assets efficiently to develop the business of the combined company;
- minimizing the diversion of management's attention from ongoing business concerns; and
- coordinating geographically separate organizations.

In addition, Computer Motion's products differ in substantial ways from Intuitive's products, and the companies rely on different distributors and sales channels to sell their products. Both Computer Motion and Intuitive Surgical are parties to existing distribution agreements that cannot be terminated prior to the end of their terms.

The combined company may not succeed in addressing these risks or any other problems encountered in connection with the merger, or whether the integration of Computer Motion with Intuitive Surgical will result in the realization of the full benefits anticipated by us from the merger.

SALES BY INTUITIVE SURGICAL STOCKHOLDERS OR FORMER COMPUTER MOTION STOCKHOLDERS COULD CAUSE INTUITIVE SURGICAL'S COMMON STOCK PRICE TO DECLINE.

The market price of our common stock could decline as a result of sales of a large number of shares in the market. These sales may also make it more difficult for the combined company to sell equity securities in the future at a time and at a price that we deem appropriate to raise funds through future offerings of common stock. As of June 30, 2003, Bear Stearns Asset Management beneficially owned more than 5% of the outstanding shares of our common stock. In connection with the acquisition, Intuitive Surgical assumed outstanding Computer Motion options and warrants and converted them into options and warrants to purchase approximately 2.2 million shares of Intuitive Surgical commons stock, including 1.4 million option shares, most of which fully vested upon completion of the merger. The employment of many of these employee option holders will be terminated as part of the Company's restructuring plan and will then have 90 days to exercise any outstanding options. After the merger closed, former stockholders of Computer Motion owned approximately 30% of our outstanding common stock.

CUSTOMER, SUPPLIER, AND EMPLOYEE UNCERTAINTY RELATED TO THE MERGER COULD HARM THE COMBINED COMPANY

Intuitive Surgical and Computer Motion customers and suppliers may, in response to the completion of the merger, delay purchasing or supply decisions or otherwise alter existing relationships with Intuitive Surgical or Computer Motion. These decisions or other adverse changes in the business relationships of Intuitive Surgical and Computer Motion with their respective customers and suppliers could adversely affect the business of the combined company. Similarly, current and prospective Computer Motion employees may experience uncertainty about their future as employees of the combined company until strategies with regard to Computer Motion are implemented. This may adversely affect the Company's ability to attract and retain, and may affect the performance during the transition period of, key management, sales, marketing and technical personnel.

THE CONVICTION OF ARTHUR ANDERSEN LLP ON OBSTRUCTION OF JUSTICE CHARGES MAY ADVERSELY AFFECT ARTHUR ANDERSEN'S ABILITY TO SATISFY CLAIMS ARISING FROM THE PROVISION OF AUDITING SERVICES TO COMPUTER MOTION AND MAY IMPEDE THE COMBINED COMPANY'S ACCESS TO CAPITAL MARKETS.

Arthur Andersen LLP audited Computer Motion's financial statements for the years ended December 31, 2001 and December 31, 2000. On March 14, 2002, an indictment was unsealed charging Arthur Andersen with federal obstruction of justice arising from the government's investigation of Enron Corp. On June 15, 2002, Arthur Andersen was convicted of these charges. The impact of this conviction on Arthur Andersen's financial condition may adversely affect the ability of Arthur Andersen to satisfy any claims arising from its provision of auditing services to Computer Motion.

Should Intuitive Surgical seek to access the public capital markets, SEC rules will require Intuitive Surgical to include or incorporate by reference in any prospectus three years of audited financial statements. The SEC's current rules would require Intuitive Surgical to present audited financial statements for one or more fiscal years audited by Arthur Andersen and use reasonable efforts to obtain its consent until the audited financial statements for the fiscal year ending December 31, 2004 become available. If prior to that time the SEC ceases accepting financial statements audited by Arthur Andersen, it is possible that the available audited financial statements for the years ended December 31, 2001 and December 31, 2000 audited by Arthur Andersen might not satisfy the SEC's requirements. In that case, Intuitive Surgical would be unable to access the public capital markets unless an independent accounting firm were able to audit the financial statements originally audited by Arthur Andersen. Any delay or inability to access the public capital markets caused by these circumstances could have a material adverse effect on the combined company's business, profitability and growth prospects.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are not subject to any meaningful market risks related to currency, commodity prices or similar matters. We are sensitive to short-term interest rate fluctuations to the extent that such fluctuations impact the interest income we receive on the investment of the remaining proceeds from our June 2000 initial public offering.

The primary objective of our investment activities is to preserve principal while at the same time maximizing the income we receive from our investments without significantly increasing risk. Some of the securities that we invest in may have market risk. This means that a change in prevailing interest rates may cause the principal amount of the investment to fluctuate. For example, if we hold a security that was issued with a fixed interest rate at the then-prevailing rate and the prevailing interest rate later rises, the principal amount of our investment will probably decline. To minimize this risk in the future, we intend to maintain our portfolio of cash equivalents and short-term investments in a variety of securities. We classify our cash equivalents and marketable securities as "fixed-rate" if the rate of return on such instruments remains fixed over their term. These "fixed-rate" investments include commercial paper and government and non-government debt securities. We classify our cash equivalents and marketable securities as "variable- rate" if the rate of return on such investments varies based on the change in a predetermined index or set of indices during their term. These "variable-rate" investments primarily include money market accounts. The average time to maturity of all of our investments as of June 30, 2003 was approximately 1.41 years. At June 30, 2003, approximately 31% of our investment portfolio was composed of investments with original maturities of one year or less.

ITEM 4. CONTROLS AND PROCEDURES

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow for timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management is required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

As required by SEC Rule 13a-15(b), we carried out an evaluation, under the supervision and with the participation of the our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the quarter covered by this report. Based on the foregoing, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective at the reasonable assurance level.

There has been no change in our internal controls over financial reporting during our most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal controls over financial reporting.

PART II. - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

BROOKHILL-WILK 1, LLC

On September 1, 2000, Brookhill-Wilk 1, LLC ("Wilk") filed a lawsuit against Intuitive Surgical in the United States District Court for the Southern District of New York (Case No. 00 Civ. 6599 (NRB)) alleging that by making, using, selling or offering for sale our *da Vinci* Surgical System, we are infringing U.S. Patent Nos. 5,217,003 and 5,368,015 in willful disregard of Wilk's patent rights. These patents concern methods and devices for "remote" surgery. In March 2001, Wilk withdrew its assertion of infringement of the '015 patent against our Company. On November 8, 2001, in response to a motion on one of Intuitive Surgical's noninfringement defenses, the District Court granted summary judgment of noninfringement of the '003 patent in our favor and dismissed Wilk's complaint in its entirety without prejudice. Wilk appealed the summary judgment ruling to the U.S. Court of Appeals for the Federal Circuit.

On April 11, 2003, the Court of Appeals reversed the District Court's judgment and remanded the case for further proceedings. This reversal is based on the Court of Appeals' determination that the particular claim limitation at issue should be interpreted differently than as construed by the District Court. The Court of Appeals has since clarified its opinion in response to Intuitive Surgical's petition for rehearing. Upon remand, Intuitive Surgical intends to continue to vigorously defend its rights and, if necessary, is prepared to continue to dispute the meaning of other portions of the asserted claim language and to conduct discovery and file further motions on whether the patent is infringed, valid and/or enforceable. Intuitive Surgical believes that it will prevail in the litigation and that it has multiple meritorious defenses to Wilk's allegations. However, litigation is unpredictable and Intuitive Surgical may not prevail. The case remains in its early stages of discovery in the District Court.

If we lose Wilk's suit against us, it will hurt our competitive position, may be costly to us and may prevent us from selling our products. If we lose the patent suit, we may need to obtain from Wilk a license to this technology if we are to continue to market our products that have been found to infringe Wilk's patents. This license could be expensive, which could seriously harm our business. If Wilk is successful in its suit against us and is unwilling to grant us a license, we may be required to stop selling our products that are found to infringe Wilk's patents unless we can redesign them so they do not infringe Wilk's patents, which we may be unable to do. In addition, we could be required to pay Wilk damages, including treble damages, which could be substantial and harm our financial position. Due to the inherent uncertainties of litigation, however, the Company cannot accurately predict the ultimate outcome of the litigation against Wilk at this time and, therefore, cannot estimate the range of possible loss.

OTHER LEGAL MATTERS

In September 2002, we discovered that one of our employees had purchased approximately $900,000 in administrative supplies without the authorization or knowledge of the Company's management. This matter was investigated by law enforcement authorities and Company advisors. We have since terminated this employee's employment and have taken actions intended to ensure that no similar incidents can occur in the future, including implementing additional controls relating to our cash disbursement process. In addition, we are seeking to recover our loss. We have filed a claim with our insurance carrier, from which we received proceeds of $500,000, and filed suit against the sellers of the administrative supplies in December 2002. Our complaint alleged that each of the defendants has (i) violated various sections of the Racketeer Influenced and Corrupt Organization ("RICO") Act through their extortion, coercion, intimidation, fraud, bribery and racketeering activity in connection with the unauthorized purchase of office supplies, and (ii) committed unlawful business acts and practices in violation of Cal. Bus. & Prof. Code Section 17200 et seq. Our suit seeks to recover actual and treble damages, costs and attorney fees for the damage caused by each of defendants through their illegal conduct. In January 2003, we amended our complaint to allege that each defendant further unlawfully offered prizes and gifts in violation of Cal. Bus. & Prof. Code Section 17537 and unlawfully failed to advertise limitations on the quantity of its sales in violation of Cal. Bus. & Prof. Code Section 17500.5. The amended complaint reiterates our claim to recover actual and treble damages, costs and attorney fees. Discovery has not yet begun. Defendants have demurred to the complaint, alleging that the complaint does not contain sufficiently pled information to support each of Intuitive's causes of action. The Court will resolve the demurrer before the case continues.

During the second quarter 2003, two former patients of The Valley Hospital in New Jersey filed suit against The Valley Hospital, their surgeon(s) and Intuitive Surgical, Inc. alleging various harms caused during their earlier surgeries. Intuitive was named because the *da Vinci* System was utilized for a portion of the complained-of surgeries and a small portion of the tip of an *EndoWrist* instrument remained in each patient after each surgery. Each suit presents multiple claims variously alleging, among others, negligence, carelessness and/or recklessness by each defendant, that the *da Vinci* System was defectively designed and manufactured, that Intuitive failed to properly instruct and train its surgeon in its use, and that the defendants failed to properly apprise the patients of the risks involved. Each suit seeks an unspecified amount of general, special and punitive damages from the defendants, in addition to a request to recover the costs of suit and attorney fees. As each suit was just recently filed, both are in very early stages and discovery has not yet begun.

We are subject to legal proceedings and claims that arise in the normal course of our business. We do not know whether we will prevail in these matters nor can we assure that any remedy could be reached on commercially viable terms, if at all. Due to the inherent uncertainties of litigation, we cannot accurately predict the ultimate outcome of these matters at this time and, therefore, cannot estimate the range of possible loss.

ITEM 2. CHANGES IN SECURITIES AND USE OF PROCEEDS

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

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

At the Annual Meeting of Stockholders held on June 30, 2003, the stockholders of Intuitive Surgical, Inc.:

1. Approved the issuance of Intuitive Surgical common stock, par value $0.001, pursuant to the agreement and plan of merger, dated March 7, 2003, by and among Intuitive Surgical, Intuitive Merger Corporation and Computer Motion, Inc. The voting results were 21,293,411 - For; 24,373 - Against; and 13,159,259 - Abstained.

2. Approved an amendment to Intuitive Surgical's Amended and Restated Certification of Incorporation to effect a 1-for-2 reverse stock split of Intuitive Surgical's common stock. The voting results were 33,912,057 - For; 439,389 - Against; and 125,597 - Abstained.

3. Elected Lonnie M. Smith, Richard J. Kramer, and James A. Lawrence to the Board of Directors of the Company to terms expiring at the Annual Meeting of Stockholders in the year 2006. The following table sets forth the votes for each director:

	Votes For	Withheld
Lonnie M. Smith	34,451,360	25,683
Richard J. Kramer	34,434,375	42,668
James A. Lawrence	31,913,499	2,563,544

4. Amended Intuitive Surgical's 2002 Non-Employee Directors' Stock Option Plan to increase the annual stock option grant for non-employee directors from 5,000 to 10,000 shares, to provide for an additional annual grant of options to purchase 5,000 shares to committee chairs and to amend the automatic share increase provision. The voting results were 15,246,601 - For; 6,058,432 - Against; and 13,172,010 - Abstained.

5. Ratified the selection of Ernst & Young, LLP as the Company's independent auditors for the current fiscal year ending December 31, 2003. The voting results were 34,294,312 - For; 164,421 - Against; and 18,310 - Abstained.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits.

Exhibit Number	Description
31	Certifications of the Company's Chief Executive Officer and Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32	Certifications of the Company's Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

(b) Reports on Form 8-K.

The Company filed a Current Report on Form 8-K on April 24, 2003 (File No. 000- 30713).

SIGNATURE

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.

INTUITIVE SURGICAL, INC.
(Registrant)
By: /s/ SUSAN K. BARNES
Susan K. Barnes
Senior Vice President, Chief Financial Officer and Assistant Secretary

Date: August 14, 2003

EXHIBIT INDEX

Exhibit Number	Description
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32	Certifications of the Company's Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Exhibit 31

Certification of Chief Executive Officer
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Lonnie M. Smith, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Intuitive Surgical, Inc.;

2. Based on my knowledge, this 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 report;

3. Based on my knowledge, the financial statements, and other financial information included in this 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 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-15(e) and 15d-15(e)) for the registrant and have:

a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, 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 report is being prepared;

b) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

c) disclosed in this report any change in the registrant's internal controls over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal controls over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal controls over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

a) all significant deficiencies and material weaknesses in the design or operation of internal controls over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; 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 over financial reporting.

Date: August 14, 2003

/s/ Lonnie M. Smith
Lonnie M. Smith
Chief Executive Officer

Certification of Chief Financial Officer
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Susan K. Barnes, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Intuitive Surgical, Inc.;

2. Based on my knowledge, this 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 report;

3. Based on my knowledge, the financial statements, and other financial information included in this 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 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-15(e) and 15d-15(e)) for the registrant and have:

a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, 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 report is being prepared;

b) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

c) disclosed in this report any change in the registrant's internal controls over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal controls over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal controls over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

a) all significant deficiencies and material weaknesses in the design or operation of internal controls over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; 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 over financial reporting.

Date: August 14, 2003

/s/ Susan K. Barnes
Susan K. Barnes
Chief Financial Officer

Exhibit 32

Certification of Chief Executive Officer
Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Pursuant to 18 U.S.C. § 1350, as created by Section 906 of the Sarbanes-Oxley Act of 2002, the undersigned officer of Intuitive Surgical, Inc. (the "Company") hereby certifies, to such officer's knowledge, that:

(i) the accompanying Quarterly Report on Form 10-Q of the Company for the quarterly period ended June 30, 2003 (the "Report") fully complies with the requirements of Section 13(a) or Section 15(d), as applicable, of the Securities Exchange Act of 1934, as amended; and

(ii) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: August 14, 2003

/s/ Lonnie M. Smith

Lonnie M. Smith

Chief Executive Officer

Certification of Chief Financial Officer
Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Pursuant to 18 U.S.C. § 1350, as created by Section 906 of the Sarbanes-Oxley Act of 2002, the undersigned officer of Intuitive Surgical, Inc. (the "Company") hereby certifies, to such officer's knowledge, that:

(i) the accompanying Quarterly Report on Form 10-Q of the Company for the quarterly period ended June 30, 2003 (the "Report") fully complies with the requirements of Section 13(a) or Section 15(d), as applicable, of the Securities Exchange Act of 1934, as amended; and

(ii) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: August 14, 2003

/s/ Susan K. Barnes

Susan K. Barnes

Chief Financial Officer