

Edgar Filing: AETHLON MEDICAL INC - Form 10QSB

AETHLON MEDICAL INC
Form 10QSB
February 19, 2003

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-QSB

(Mark One)

0

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

For the quarterly period ended December 31, 2002

OR

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

For the transition period from _____ to _____

COMMISSION FILE NUMBER 0-21846

AETHLON MEDICAL, INC.

(Exact name of registrant as specified in its charter)

NEVADA

13-3632859

State or other jurisdiction of
incorporation or organization)

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

7825 FAY AVENUE, SUITE 200, LA JOLLA, CA

92037

(Address of principal executive offices)

(Zip Code)

(858) 456-5777

(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 such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No X .

The number of shares of common stock of the registrant outstanding as of February 11, 2003 was 5,921,052.

PART I. FINANCIAL INFORMATION

ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Condensed Consolidated Balance Sheets at December 31, 2002 (unaudited) and March 31, 2002

Edgar Filing: AETHLON MEDICAL INC - Form 10QSB

Condensed Consolidated Statements of Operations (unaudited) for the three and nine months ended December 31, 2002 and 2001 and for the period January 31, 1984 (Inception) through December 31, 2002

Condensed Consolidated Statements of Cash Flows (unaudited) for the nine months ended December 31, 2002 and 2001 and for the period January 31, 1984 (Inception) through December 31, 2002

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

ITEM 3. CONTROLS AND PROCEDURES

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

ITEM 2. CHANGES IN SECURITIES

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

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

ITEM 5. OTHER INFORMATION

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

2

PART I. FINANCIAL INFORMATION

All references to "us", "we", "Aethlon", "Aethlon Medical", or "the Company" refer to Aethlon Medical, Inc., its predecessors and its subsidiaries.

ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

AETHLON MEDICAL, INC. AND SUBSIDIARIES (A Development Stage Company) CONDENSED CONSOLIDATED BALANCE SHEETS

	December 31, 2002 (Unaudited)	March 31, 2002
	-----	-----
ASSETS		
Current Assets		
Cash	\$ 14,446	\$ 10,667
Prepaid expenses	23,771	140,788
Other current assets	2,150	--
	-----	-----
	40,367	151,455
Furniture and Equipment, net	22,048	37,182
Patents and Patents Pending, net	592,198	560,790
Employment Contract, net	126,945	222,156

Edgar Filing: AETHLON MEDICAL INC - Form 10QSB

Other Assets	1,955	1,955
	-----	-----
	\$ 783,513	\$ 973,538
	=====	=====

LIABILITIES AND STOCKHOLDERS' DEFICIT

Current Liabilities

Accounts payable and accrued liabilities	\$ 1,202,006	\$ 1,160,219
Due to related parties	1,344,530	1,073,355
Notes payable	487,500	572,500
Convertible notes payable	680,000	365,000
	-----	-----
	3,714,036	3,171,074

Commitments and Contingencies

Stockholders' Deficit

Common stock, par value \$0.001 per share; 25,000,000 shares authorized; 5,633,052 and 5,170,697 shares issued and outstanding at December 31, 2002 and March 31, 2002, respectively	5,633	5,171
Additional paid-in capital	8,020,775	7,391,382
Stock options and warrants	3,660,596	3,571,310
Deficit accumulated during development stage	(14,617,527)	(13,165,399)
	-----	-----
	(2,930,523)	(2,197,536)
	-----	-----
	\$ 783,513	\$ 973,538
	=====	=====

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

AETHLON MEDICAL, INC. AND SUBSIDIARIES (A Development Stage Company)

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

For the Three and Nine Months Ended December 31, 2002 and 2001 and For the Period January 31, 1984 (Inception) Through December 31, 2002

(Unaudited)

THREE MONTHS ENDED DECEMBER 31, 2002	THREE MONTHS ENDED DECEMBER 31, 2001	NINE MONTHS ENDED DECEMBER 31, 2002	NINE MONTHS ENDED DECEMBER 31, 2001
-----	-----	-----	-----

Edgar Filing: AETHLON MEDICAL INC - Form 10QSB

REVENUES				
Grant income	\$	--	\$	--
Subcontract income		--		--
Sale of research and development		--		--
		-----		-----
		--		--
EXPENSES				
Personnel		103,635		147,594
Professional fees		165,654		176,539
Rent		15,921		14,502
Depreciation		5,351		5,465
Amortization of goodwill		--		--
Other amortization		31,737		33,779
Impairment of goodwill		--		--
Other expenses		33,172		26,574
		-----		-----
		355,470		404,453
				1,149,293
				1,337,984
OTHER EXPENSE (INCOME)				
Interest and other debt expenses		50,849		216,169
Other charge		--		--
Other income		--		(1,616)
Interest income		(42)		(42)
		-----		-----
		50,807		216,169
				302,835
				661,891
NET LOSS BEFORE PROVISION FOR INCOME TAXES				
		(406,277)		(620,622)
				(1,452,128)
				(1,999,875)
PROVISION FOR INCOME TAXES				
		--		--
		-----		-----
		--		--
NET LOSS				
		(\$ 406,277)		(\$ 620,622)
		=====		=====
				(\$ 1,452,128)
				(\$ 1,999,875)
BASIC AND DILUTED LOSS PER COMMON SHARE				
		(\$ 0.07)		(\$ 0.17)
		=====		=====
				(\$ 0.27)
				(\$ 0.55)
WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING				
		5,586,904		3,756,327
		=====		=====
				5,433,046
				3,614,506

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

Edgar Filing: AETHLON MEDICAL INC - Form 10QSB

(Unaudited)

	Nine Months Ended December 31, 2002	Nine Months Ended December 31, 2001	January 31, 1984 (Inception) Through December 31, 2002
	-----	-----	-----
CASH FLOWS FROM OPERATING ACTIVITIES			
Net loss	\$ (1,452,128)	\$ (1,999,875)	\$ (14,617,527)
Adjustments to reconcile net loss to net cash used in operating activities:			
Depreciation and amortization	118,897	160,839	742,029
Gain on sale of furniture and equipment	--	--	(13,065)
Interest and debt expenses related to warrants	(24,714)	227,291	2,590,022
Common stock, warrants and options issued for services	159,000	236,170	2,030,434
Beneficial conversion feature of convertible notes payable	245,700	128,000	580,700
Impairment of goodwill	--	--	897,227
Deferred compensation forgiven	--	--	217,223
Changes in operating assets and liabilities:			
Accounts receivable	--	4,689	--
Prepaid expenses	117,017	6,934	137,766
Other assets	(2,150)	--	(4,105)
Accounts payable and accrued liabilities	179,442	311,088	1,339,661
Due to related parties	296,175	152,169	1,369,530
	-----	-----	-----
Net cash used in operating activities	(362,761)	(772,695)	(4,730,105)
CASH FLOWS FROM INVESTING ACTIVITIES			
Acquisition of furniture and equipment	(1,197)	(30,804)	(209,383)
Acquisition of patents and patents pending	(38,763)	(40,471)	(342,562)
Proceeds from sale of furniture and equipment	--	--	17,065
Cash of acquired company	--	--	10,728
	-----	-----	-----
Net cash used in investing activities	(39,960)	(71,275)	(524,152)

(continued)

5

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

AETHLON MEDICAL, INC. AND SUBSIDIARIES
(A Development Stage Company)
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
For the Six Months Ended December 31, 2002 and 2001 and For the Period January
31, 1984 (Inception) Through December 31, 2002

(Unaudited)

Edgar Filing: AETHLON MEDICAL INC - Form 10QSB

	Nine Months Ended December 31, 2002	Nine Months Ended December 31, 2001	January 31, 1984 (Inception) Through December 31, 2002
	-----	-----	-----
CASH FLOWS FROM FINANCING ACTIVITIES			
Proceeds from issuance of notes payable	\$ 340,000	\$ 128,000	\$ 2,278,000
Principal payments of notes payable	(35,000)	--	(35,000)
Net proceeds from issuance of common stock	101,500	711,764	3,025,703
	-----	-----	-----
Net cash provided by financing activities	406,500	839,764	5,268,703
	-----	-----	-----
NET (DECREASE) INCREASE IN CASH	3,779	(4,206)	14,446
CASH - beginning of period	10,667	6,058	--
	-----	-----	-----
CASH - end of period	\$ 14,446	\$ 1,852	\$ 14,446
	=====	=====	=====

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

6

AETHLON MEDICAL, INC. AND SUBSIDIARIES (A Development Stage Company) NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS December 31, 2002

NOTE 1. NATURE OF BUSINESS AND BASIS OF PRESENTATION

Aethlon Medical, Inc. (the "Company") engages in the research and development of a medical device known as the Hemopurifier(TM) that removes harmful substances from the blood. The Company is in the development stage on the Hemopurifier and significant research and testing are still needed to reach commercial viability. Any resulting medical device or process will require approval by the U.S. Food and Drug Administration ("FDA"), and the Company has not yet begun efforts to obtain FDA approval on its current lead product candidate, which may take several years. Since many of the Company's patents were issued in the 1980's, they are scheduled to expire in the near future. Thus, such patents may expire before FDA approval, if any, is obtained.

The Company is classified as a development stage enterprise under accounting principles generally accepted in the United States ("GAAP"), and has not generated revenues from its principal operations.

The Company's common stock is quoted on the Over-the-Counter Bulletin Board of the National Association of Securities Dealers under the symbol "AEMD".

The accompanying unaudited condensed consolidated financial statements of

Edgar Filing: AETHLON MEDICAL INC - Form 10QSB

Aethlon Medical, Inc. (the "Company") have been prepared in accordance with GAAP for interim financial information and with the instructions to Form 10-QSB. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three-month and nine-month periods ended December 31, 2002 are not necessarily indicative of the results that may be expected for the year ending March 31, 2003. For further information, refer to the Company's Annual Report on Form 10-KSB for the year ended March 31, 2002, which includes audited financial statements and footnotes as of and for the years ended March 31, 2002 and 2001.

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The summary of significant accounting policies of the Company presented below is designed to assist the reader in understanding the Company's consolidated financial statements. Such financial statements and related notes are the representations of Company management, who is responsible for their integrity and objectivity. These accounting policies conform to GAAP in all material respects, and have been consistently applied in preparing the accompanying condensed consolidated financial statements.

PRINCIPLES OF CONSOLIDATION

The accompanying condensed consolidated financial statements include the accounts of Aethlon Medical, Inc. and its legal wholly-owned subsidiaries Aethlon, Inc., Hemex, Inc. and Cell Activation, Inc. ("Cell") (collectively hereinafter referred to as the "Company"). All significant intercompany balances and transactions have been eliminated in consolidation.

7

AETHLON MEDICAL, INC. AND SUBSIDIARIES (A Development Stage Company) NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS December 31, 2002

LOSS PER COMMON SHARE

Loss per common share is based on the weighted average number of shares of common stock and common stock equivalents outstanding during the year in accordance with Statement of Financial Accounting Standards No. 128, "Earnings per Share."

Securities that could potentially dilute basic loss per share (prior to their conversion, exercise or redemption) were not included in the diluted-loss-per-share computation because their effect is anti-dilutive. The total potential common shares that have not been included in such computation are approximately 4,150,000 at December 31, 2002.

RECENT ACCOUNTING PRONOUNCEMENTS

In July 2001, the FASB issued Statements No. 141, "Business Combinations" ("SFAS 141") and No. 142 "Goodwill and Other Intangible Assets" ("SFAS 142"). SFAS 141 is effective for fiscal years beginning after June 30, 2001 and

Edgar Filing: AETHLON MEDICAL INC - Form 10QSB

requires that all business combinations be accounted for by the purchase method. SFAS 142 provides that all existing and newly acquired goodwill and certain intangible assets will no longer be amortized but will be tested for impairment at least annually and written down only when impaired. Additionally, the FASB has recently issued Statements No. 143, "Accounting for Asset Retirement Obligations" ("SFAS 143") and No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS 144"). SFAS 143 addresses financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs, and is effective for financial statements issued for fiscal years beginning after June 15, 2002. For the three-month period ended June 30, 2002, the Company adopted SFAS 141, 142 and 144. There was no significant effect on the Company's June 30, 2002 financial statements. Management does not expect that the requirements of SFAS 143 will have a significant impact on the Company's future financial statements.

In December 2002, the FASB issued SFAS 148, "Accounting for Stock-Based Compensation - Transition and Disclosure" an amendment of FASB Statement No. 123, "which is effective for fiscal years beginning after December 15, 2002. SFAS 148 provides alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. In addition, this Statement amends the disclosure requirements of Statement 123 to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based employee compensation and the effect of the method used on reported results. Management has not determined the effect, if any, of SFAS 148 on the Company's future financial statements.

RECLASSIFICATIONS

Certain reclassifications have been made to the December 31, 2001 financial statement presentation to correspond to the December 31, 2002 format.

8

AETHLON MEDICAL, INC. AND SUBSIDIARIES (A Development Stage Company) NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS December 31, 2002

NOTE 3. CONVERTIBLE NOTES PAYABLE

CONVERTIBLE NOTES

On July 2, 2002, the Company issued a convertible note in the amount of \$50,000 to an investor bearing interest at 10% per annum, with principal and interest thereon due January 3, 2003. On August 9, 2002, the Company issued a convertible note in the amount of \$50,000 to an investor bearing interest at 10% per annum, with principal and interest thereon due February 10, 2003. On August 15, 2002, the Company issued a convertible note in the amount of \$50,000 to an investor bearing interest at 10% per annum, with principal and interest thereon due February 16, 2003. All three notes may be converted to common stock of the Company at any time at the option of the respective holder at the conversion price of \$0.50 per share. A beneficial conversion feature approximating \$150,000 was recorded during the quarter ended September 30, 2002. In the three months ended December 31, 2002, the Company issued five convertible notes totaling \$45,000 with the right of the noteholders to convert to common stock at a

Edgar Filing: AETHLON MEDICAL INC - Form 10QSB

conversion price of \$0.50 per share. During the quarter, an existing noteholder increased its advances to the Company by \$40,000 to a total of \$140,000. In consideration, the Company granted the noteholder a warrant to purchase 580,000 shares of common stock at a price of \$0.25 per share and a security interest in certain assets of the Company. The new note bears interest at 10% per annum, with principal and interest thereon due April 30, 2003. A beneficial conversion feature approximating \$15,700 was recorded during the quarter ended December 31, 2002.

The Company is currently in default on approximately \$857,500 of amounts owed under various notes payable and is currently seeking other financing arrangements to retire all past due notes.

NOTE 4. GOING CONCERN AND LIQUIDITY CONSIDERATIONS

The accompanying condensed consolidated financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the satisfaction of liabilities in the ordinary course of business. The Company has experienced a loss of approximately \$15 million for the period from January 31, 1984 (Inception) through December 31, 2002. The Company has not generated significant revenue or any profit from operations since inception. A substantial amount of additional capital will be necessary to advance the development of the Company's products to the point at which they may become commercially viable. Such factors indicate that the Company may be unable to continue as a going concern for a reasonable period of time. Management is in discussions with potential investors to pursue additional capital infusions into the Company, which management believes are necessary at least until such time that the Company generates sufficient revenues and achieves profitability and positive cash flow.

The condensed consolidated financial statements do not include any adjustments relating to the recoverability of assets that might be necessary should the Company be unable to continue as a going concern. The Company's continuation as a going concern is dependent upon its ability to obtain additional financing as may be required, and generate sufficient revenue and operating cash flow to meet its obligations on a timely basis.

NOTE 5. COMMITMENTS AND CONTINGENCIES

REGISTRATION RIGHTS AGREEMENTS

The Company is obligated under various agreements to register its common stock, including the common stock underlying certain warrants and options. The Company is subject to penalties for failure to register such securities, the amount of which could be material to the Company's financial position, results of operations and cash flows. The Company filed a registration statement on Form SB-2 with the Securities and Exchange Commission in December 2000 to register the necessary securities. However, such registration statement was never declared effective. Management is currently unaware of any potential claims related to the lack of registration and plans to file a revised registration statement as funds to cover registration expenses become available. The Company may incur additional charges in exchange for further waivers through the date of an effective registration statement.

Edgar Filing: AETHLON MEDICAL INC - Form 10QSB

December 31, 2002

DELINQUENT SEC FILING

The Company's March 31, 2002 Form 10-KSB did not contain certain disclosure items in its Executive Compensation, Security Ownership of Certain Beneficial Owners and Management and Certain Relationships and Related Transactions. Such sections were intended to be incorporated by reference in the Company's proxy statement, which was not filed. The failure to file the proxy statement with the disclosures required in Form 10-KSB constitutes non-compliance with the periodic reporting requirements of the Securities and Exchange Act of 1934 (the "Exchange Act") and, among other things, could result in de-listing of the Company's common stock from the Over-the-Counter Bulletin Board ("OTCBB").

In addition, any owners of the Company's restricted securities who are otherwise eligible to sell such securities under Rule 144 may be temporarily unable to do so until such filing delinquency is cured. The Company intends to file an amendment to its Annual Report on Form 10-KSB for the year ended March 31, 2002 to cure such delinquency.

NOTE 6. STOCK TRANSACTIONS

In January 2002, the Company entered into a consulting agreement under which the consultant was granted an option to purchase up to 400,000 shares of restricted common stock of the Company at the exercise price of \$0.50 per share, expiring January 2003. On February 12, 2002, the consultant exercised all 400,000 options. Such options were valued at approximately \$562,000, using the Black-Scholes option pricing model. In July 2002, the Company extended the original agreement by six months to expire July 2003. As a result of extending the agreement, the consultant received an additional option to purchase up to 200,000 shares of restricted common stock of the Company at the exercise price of \$0.50 per share. During the quarter ended September 30, 2002, the Company issued 148,000 shares of restricted common stock in exchange for \$74,000 in cash under such agreement. Such options were valued at approximately \$114,000 using the Black-Scholes option pricing model all of which was charged to expense in the accompanying condensed consolidated statements of operations and \$57,000 is included in prepaid expenses at September 30, 2002. \$57,000 was charged to expense in the accompanying condensed consolidated statements of operations.

In October 2002, the Company issued 52,000 shares of Restricted Common Stock in connection with the exercise of options for cash totaling \$26,000. In addition, in November 2002, a consultant was issued 3000 shares of Restricted Common Stock in consideration for cash of \$1,500. Also in November, 2002, 69,231 shares were issued to another consultant in consideration of services performed valued at approximately \$45,000.

NOTE 7. SUBSEQUENT EVENTS

In January and February 2003, investors purchased 288,000 shares of the Company's Restricted Common Stock for cash totaling \$80,000.

In February 2003, a complaint was filed against the Company to collect a past due note. The plaintiff seeks repayment of past due principal and interest of approximately \$65,000. The plaintiff also asserts that the Company violated state and federal securities laws and claims that the Company committed fraud in the issuance of the note. While the Company admits that it borrowed money from the plaintiff and that the note is past due, the Company disputes the plaintiff's allegations concerning state and federal securities law violations and fraud.

The Company has not yet answered this complaint and is seeking to settle the

Edgar Filing: AETHLON MEDICAL INC - Form 10QSB

lawsuit by repaying the indebtedness. The Company has accrued such amount in the accompanying condensed consolidated financial statements.

10

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

The following discussion of Aethlon Medical's financial condition and results of operations should be read in conjunction with, and is qualified in its entirety by the condensed consolidated financial statements and notes thereto, included in Item 1 in this Quarterly Report on Form 10-QSB. This item contains forward-looking statements that involve risks and uncertainties. Actual results may differ materially from those indicated in such forward-looking statements.

FORWARD LOOKING STATEMENTS

All statements, other than statements of historical fact, included in this Form 10-QSB are, or may be deemed to be, "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended ("the Securities Act"), and Section 21E of the Exchange Act. Such forward-looking statements involve assumptions, known and unknown risks, uncertainties and other factors which may cause the actual results, performance, or achievements of Aethlon Medical, Inc. ("the Company") to be materially different from any future results, performance, or achievements expressed or implied by such forward looking statements contained in this Form 10-QSB. Such potential risks and uncertainties include, without limitation, completion of the Company's capital-raising activities, FDA approval of the Company's products, other regulations, patent protection of the Company's proprietary technology, product liability exposure, uncertainty of market acceptance, competition, technological change, and other risk factors detailed herein and in other of the Company's filings with the Securities and Exchange Commission. The forward-looking statements are made as of the date of this Form 10-QSB, and the Company assumes no obligation to update the forward-looking statements, or to update the reasons actual results could differ from those projected in such forward-looking statements.

THE COMPANY

Aethlon Medical is a development stage therapeutic device company that has not yet engaged in significant commercial activities. We are continuing to devote a significant portion of our resources to the advancement of our research and development efforts and are developing new treatments for the removal of targeted viruses and other intoxicants from the blood based on our proprietary Hemopurifier(TM) platform technology. Our main focus during fiscal 2002 was to further advance the HIV-Hemopurifier, know as AEMD-45.

Our principal executive office is located at 7825 Fay Avenue, Suite 200, La Jolla, California 92037. Our telephone number is 858/456-5777, and our website is www.aethlonmedical.com.

We file annual, quarterly, special reports, proxy statements and other information with the Securities Exchange Commission (SEC). Reports, proxy statements and other information filed with the SEC can be inspected and copied at the public reference facilities of the SEC at 450 Fifth Street NW, Washington, DC 20549. Such material may also be accessed electronically by means of the SEC's website at www.sec.gov.

Edgar Filing: AETHLON MEDICAL INC - Form 10QSB

Our common stock, par value \$0.001 per share, is traded on the OTCBB under the symbol "AEMD".

CRITICAL ACCOUNTING POLICIES

The preparation of condensed consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires us to make a number of estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements. Such estimates and assumptions affect the reported amounts of expenses during the reporting period. On an ongoing basis, we evaluate estimates and assumptions based upon historical experience and various other factors and circumstances. We believe our estimates and assumptions are reasonable in the circumstances; however, actual results may differ from these estimates under different future conditions.

We believe that the estimates and assumptions that are most important to the portrayal of our financial condition and results of operations, in that they require our most difficult, subjective or complex judgments, form the basis for the accounting policies deemed to be most critical to us. These critical accounting policies relate to stock purchase warrants issued with notes payable, beneficial conversion feature of convertible notes payable, impairment of intangible assets and long lived assets, contingencies and litigation. We believe estimates and assumptions related to these critical accounting policies are appropriate under the circumstances; however, should future events or occurrences result in unanticipated consequences, there could be a material impact on our future financial conditions or results of operations.

11

RESULTS OF OPERATIONS

THE THREE MONTHS ENDED DECEMBER 31, 2002 COMPARED TO THE THREE MONTHS ENDED DECEMBER 31, 2001.

OPERATING EXPENSES

Consolidated operating expenses were \$355,470 for the three months ended December 31, 2002, versus \$404,453 for the comparable period ended December 31, 2001. This decrease of 12.1% in operating expenses is principally attributable to decreased professional fees and personnel expenses due to reduced professionals associated with strategic and financial planning activities reduced staff.

NET LOSS

We recorded a consolidated net loss of (\$406,277) and (\$620,622) for the quarters ended December 31, 2002 and 2001, respectively. The decrease in net loss of 34.5% was primarily attributable to decreased professional fees and personnel expenses and decreased financing costs associated with warrants and debt conversions.

Basic and diluted loss per common share were (\$0.07) for the three month period ended December 31, 2002 compared to (\$0.17) for the same period ended December

Edgar Filing: AETHLON MEDICAL INC - Form 10QSB

31, 2001, representing a reduction in basic and diluted loss per share of 58.8%. This reduction in loss per share was primarily attributable to the decreased personnel, professional and financing costs, as well as the increase in the weighted average number of shares outstanding during the three month period ended December 31, 2002, as compared to the three month period ended December 31, 2001.

THE NINE MONTHS ENDED DECEMBER 31, 2002 COMPARED TO THE NINE MONTHS ENDED DECEMBER 31, 2001.

OPERATING EXPENSES

Consolidated operating expenses were \$1,149,293 for the nine months ended December 31, 2002, versus \$1,337,984 for the comparable period ended December 31, 2001. This decrease of 14.1% in operating expenses is primarily attributable to decreased professional fees, amortization and other expenses, due to relatively fewer professionals associated with strategic and financial planning activities as well as decreased personnel expenses due to reduced staff. .

We continue to carefully control costs and are pursuing various funding alternatives to support our business plan going forward.

NET LOSS

We recorded a consolidated net loss of (\$1,452,128) and (\$1,999,875) for the nine-month periods ended December 31, 2002 and 2001, respectively. The decrease in net loss of 27.4% was primarily attributable to decreases in professional fees and financing costs, plus decreases in other expenses, amortization and personnel expenses.

Basic and diluted loss per common share were (\$0.27) for the nine month period ended December 31, 2002 compared to (\$0.55) for the same period ended December 31, 2001, representing a reduction in basic and diluted loss per share of 50.9%. This reduction in loss per share was primarily attributable to the decreased professional, financing and other costs, as well as the increase in the the weighted average number of shares outstanding during the nine month period ended December 31, 2002 as compared the nine month period ended December 31, 2001.

11

LIQUIDITY AND CAPITAL RESOURCES

To date, we have funded our capital requirements for the current operations from net funds received from the public and private sale of debt and equity securities, as well as from the issuance of common stock in exchange for services. Our cash position at December 31, 2002 was \$14,446 as compared to \$10,667, at March 31, 2002, representing an increase of 35.4%.

During the nine months ended December 31, 2002, operating activities used net cash of \$362,761. We received \$101,500 from the sale of common stock. In addition, during the nine months ended December 31, 2002, we received \$340,000 from notes payable issued. During the nine month period ended December 31, 2002, net cash used in operating activities primarily consisted of net loss of \$(1,452,128). Net loss was offset by the change in other net assets (excluding cash) of \$590,484 and was increased by interest and debt expenses related to warrants of \$24,714. This change in net assets (excluding cash) was offset by -

Edgar Filing: AETHLON MEDICAL INC - Form 10QSB

\$159,000 in common stock paid for services in lieu of cash, - \$245,700 in beneficial conversion feature of convertible notes payable, and - \$118,897 in depreciation and amortization.

Changes in current assets and current liabilities resulted in a negative working capital position of (\$3,673,669) at December 31, 2002 as compared to a negative working capital of (\$3,019,619) at March 31, 2002. Our current deficit in working capital requires us to obtain funds in the short-term to be able to continue in business, and in the longer term to fund research and development on products not yet ready for market. We are seeking to fund these and other operating needs in the next 12 months from funds to be obtained through a corporate acquisition of or merger with another entity with greater financial resources, or from the proceeds of additional private placements or public offerings of debt or equity securities, or both.

Due to the our recurring losses from operations, and continued need for capital, our independent certified public accountants have included an explanatory paragraph in their audit report in the Company's Form 10-KSB at March 31, 2002 stating that these factors raise substantial doubt about the Company's ability to continue as a going concern.

During the fiscal year ended March 31, 2001, we financed our operations through the private placement of approximately \$1,365,000 of notes bearing interest at 12% per annum and convertible notes in the amount of \$395,000 bearing interest at 8% per annum. During fiscal 2002, all of the 12% notes matured, increasing the interest to 15% per annum.

In March 2002, the Company extended an offer to the 12% note holders and certain vendors to convert past due amounts into restricted common stock and warrants to purchase common stock of the Company. During the year ended March 31, 2002, note holders and vendors representing liabilities in the aggregate amount of approximately \$1,020,000 converted their debt and approximately \$238,000 in additional liabilities were converted subsequent to the fiscal year ended March 31, 2002.

During the fourth quarter of fiscal year 2001, we entered into a subscription agreement under which we received gross proceeds of approximately \$856,000, of which \$712,000, net of \$44,000 in issuance costs, were received during the first half of fiscal year 2002. The proceeds were used in part to fund operating expenses as well as to reduce existing accounts payable and related party liabilities.

During fiscal year ended March 31, 2002, we continued to issue promissory notes and convertible notes totaling \$178,000. During the nine month period ended December 31, 2002, we issued promissory notes and convertible notes totaling \$340,000. Additional funds in the aggregate amount of \$200,000 were generated in January and February 2002, through the exercise of an option to purchase 400,000 shares of the Company's restricted common stock by a consultant. During the quarter ended September 30, 2002, funds totaling \$74,000 were received from the same consultant through the exercise of an option to purchase 148,000 shares of the Company's restricted common stock. During the quarter ended December 31, 2002, funds totaling \$27,500 were received from the same consultant through the exercise of options and purchases of common stock totaling 55,000 shares of the Company's common stock.

We expect to raise additional capital within the next three months to fund research and development and other activities. Our operations to date have

Edgar Filing: AETHLON MEDICAL INC - Form 10QSB

consumed substantial capital without generating revenues, and we will continue to require substantial and increasing capital funds to conduct necessary research and development and pre-clinical and clinical testing of our Hemopurifier products, and to market any of those products that receive regulatory approval. We do not expect to generate revenue from operations for the foreseeable future, and our ability to meet our cash obligations as they become due and payable is expected to depend for at least the next several years on our ability to sell securities, borrow funds or a combination thereof. Our future capital requirements will depend upon many factors, including progress with pre-clinical testing and clinical trials, the number and breadth of our programs, the time and costs involved in preparing, filing, prosecuting, maintaining and enforcing patent claims and other proprietary rights, the time and costs involved in obtaining regulatory approvals, competing technological and market developments, and our ability to establish collaborative arrangements, effective commercialization, marketing activities and other arrangements. We expect to continue to incur increasing negative cash flows and net losses for the foreseeable future.

Management does not believe that inflation has had or is likely to have any material impact on the Company's limited operations.

At the date of this report, we do not have plans to purchase significant amounts of equipment or hire significant numbers of employees prior to successfully raising additional capital.

ITEM 3. CONTROLS AND PROCEDURES

The Company's Chief Executive Officer and Chief Financial Officer/Principal Accounting Officer (collectively, the "Certifying Officers") are responsible for establishing and maintaining disclosure controls and procedures for the Company. Such officers have concluded (based upon their evaluation of these controls and procedures as of a date within 90 days of the filing of this report) that the Company's disclosure controls and procedures are effective to ensure that information required to be disclosed by the Company in this report is accumulated and communicated to the Company's management, including its principal executive officers as appropriate, to allow timely decisions regarding required disclosure.

The Certifying Officers also have indicated that there were no significant changes in the Company's internal controls or other factors that could significantly affect such controls subsequent to the date of their evaluation, and there were no corrective actions with regard to significant deficiencies and material weaknesses.

13

PART II

OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

In February 2003, a complaint was filed against the Company to collect a past due note. The plaintiff seeks repayment of past due principal and interest of approximately \$65,000. The plaintiff also asserts that the Company violated state and federal securities laws and claims that the Company committed fraud in the issuance of the note. While the Company admits that it borrowed money from the plaintiff and that the note is past due, the Company disputes the

Edgar Filing: AETHLON MEDICAL INC - Form 10QSB

plaintiff's allegations concerning state and federal securities law violations and fraud.

The Company has not yet answered this complaint and is seeking to settle the lawsuit by repaying the indebtedness. The Company has accrued such amount in the accompanying condensed consolidated financial statements.

ITEM 2. CHANGES IN SECURITIES

The Company issued 462,355 unregistered shares of common stock during the nine month period ended December 31, 2002. Such shares were not registered under the Securities Act of 1933, as amended, in reliance upon an exemption from its registration requirements. In January and February 2003, investors purchased 288,000 shares of the Company's Restricted Common Stock for cash totaling \$80,000.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

As of the date of this report, various promissory and convertible notes payable in the aggregate principal amount of \$857,500 have reached maturity and are past due. The Company is currently seeking other financing arrangements to retire all past due notes.

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

None

ITEM 5. OTHER INFORMATION

None

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits. The following documents are filed as part of this report:

Pursuant to 18 U.S.C. ss.1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, 99.1 Certification of the Chief Executive Officer 99.2 Certification of the Chief Financial Officer

(b) Reports on Form 8-K filed during the quarter ended December 31, 2002.

None

14

SIGNATURES

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

AETHLON MEDICAL, INC

Date: February 19, 2003

BY: /S/ JAMES A. JOYCE

JAMES A. JOYCE

BY: /S/ EDWARD C. HALL

EDWARD C. HALL

Edgar Filing: AETHLON MEDICAL INC - Form 10QSB

CHAIRMAN, PRESIDENT AND
CHIEF EXECUTIVE OFFICER

CHIEF FINANCIAL OFFICER

AETHLON MEDICAL, INC.

15

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

I, James A. Joyce, certify that:

1. I have reviewed this quarterly report on Form 10-QSB of Aethlon Medical, Inc.;

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

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

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

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

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

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

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

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

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

6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal

Edgar Filing: AETHLON MEDICAL INC - Form 10QSB

controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

/s/ James A. Joyce

February 19, 2003

James A. Joyce
Chairman, President and CEO

Date

16

AETHLON MEDICAL, INC.

Certification of Chief Financial Officer/Principal Accounting Officer Pursuant to Section 302(a) of the Sarbanes-Oxley Act of 2002

I, Edward C. Hall, certify that:

1. I have reviewed this quarterly report on Form 10-QSB of Aethlon Medical, Inc.;

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

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

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

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

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

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

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

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

Edgar Filing: AETHLON MEDICAL INC - Form 10QSB

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

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

/s/ Edward C. Hall

February 19, 2003

Edward C. Hall

Date

CFO/Principal Accounting Officer