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AETHLON MEDICAL INC
Form 10QSB
August 19, 2002

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-QSB

(Mark One)

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

For the quarterly period ended June 30, 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

State or other jurisdiction of
incorporation or organization)

13-3632859

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

7825 FAY AVENUE, SUITE 200, LA JOLLA, CA

(Address of principal executive offices)

92037

(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 .
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The number of shares of common stock of the registrant outstanding as of
June 30, 2002 was 5,360,821.

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PART I.	FINANCIAL INFORMATION	
ITEM 1.	Condensed Consolidated Financial Statements	3
	Condensed Consolidated Balance Sheets at June 30, 2002 (unaudited) and March 31, 2002	3
	Condensed Consolidated Statements of Operations (unaudited) for the three months ended June 30, 2002 and June 30, 2001	4
	Condensed Consolidated Statements of Cash Flows (unaudited) for the three months ended June 30, 2002 and June 30, 2001	5
	Notes to Condensed Consolidated Financial Statements	7
ITEM 2.	Management's Discussion and Analysis or Plan of Operation	11
PART II.	OTHER INFORMATION	
ITEM 1.	Legal Proceedings	13
ITEM 2.	Changes in Securities	13
ITEM 3.	Defaults Upon Senior Securities	13
ITEM 4.	Submission of Matters to a Vote of Security Holders	13
ITEM 5.	Other Information	13
ITEM 6.	Exhibits and Reports on Form 8-K	13
SIGNATURES		14

2

PART I

FINANCIAL INFORMATION

ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

AETHLON MEDICAL, INC. AND SUBSIDIARIES
(A Development Stage Company)
CONDENSED CONSOLIDATED BALANCE SHEETS
June 30, 2002 and March 31, 2002

June 30, 2002 (Unaudited)	March 31, 2002
-----	-----

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ASSETS

Current Assets		
Cash	\$ 507	\$ 10,667
Prepaid expenses	94,540	140,788
	-----	-----
	95,047	151,455
Furniture and Equipment, net	31,717	37,182
Patents and Patents Pending, net	568,099	560,790
Employment Contract, net	190,419	222,156
Other Assets	1,955	1,955
	-----	-----
	\$ 887,237	\$ 973,538
	=====	=====

LIABILITIES AND STOCKHOLDERS' DEFICIT

Current Liabilities		
Accounts payable and accrued liabilities	\$ 1,100,926	\$ 1,160,219
Due to related parties	1,172,573	1,073,355
Notes payable	472,500	572,500
Convertible notes payable	445,000	365,000
	-----	-----
	3,190,999	3,171,074
Commitments and Contingencies		
Stockholders' Deficit		
Common stock, par value \$0.001 per share; 25,000,000 shares authorized; 5,360,821 and 5,170,697 shares issued and outstanding at June 30, 2002 and March 31, 2002, respectively	5,361	5,171
Additional paid-in capital	7,708,847	7,391,382
Stock options and warrants	3,546,596	3,571,310
Deficit accumulated during development stage	(13,564,566)	(13,165,399)
	-----	-----
	(2,303,762)	(2,197,536)
	-----	-----
	\$ 887,237	\$ 973,538
	=====	=====

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

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CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
 For the Three Months Ended June 30, 2002 and
 2001 and For the Period January 31, 1984
 (Inception) Through June 30, 2002

(Unaudited)

	Three Months Ended June 30, 2002	Three Months Ended June 30, 2001	January 31, 1984 (Inception) Through June 30, 2002
<hr style="border-top: 1px dashed black;"/>			
REVENUES			
Grant income	\$ -	\$ -	\$ 1,424,012
Subcontract income	-	-	73,746
Sale of research and development	-	-	35,810
	<hr style="border-top: 1px dashed black;"/>	<hr style="border-top: 1px dashed black;"/>	<hr style="border-top: 1px dashed black;"/>
	-	-	1,533,568
EXPENSES			
Personnel	133,442	118,377	4,736,855
Professional fees	110,347	231,238	2,776,237
Other amortization	35,414	75,419	384,405
Rent	16,030	20,622	689,923
Depreciation	5,465	6,930	179,914
Amortization of goodwill	-	-	99,692
Impairment of goodwill	-	-	897,227
Other expenses	16,826	53,609	1,637,445
	<hr style="border-top: 1px dashed black;"/>	<hr style="border-top: 1px dashed black;"/>	<hr style="border-top: 1px dashed black;"/>
	317,524	506,195	11,401,698
OTHER EXPENSE (INCOME)			
Interest and other debt expenses	83,259	153,387	3,577,860
Other charges	-	-	211,758
Other income	(1,616)	-	(75,767)
Interest income	-	-	(17,415)
	<hr style="border-top: 1px dashed black;"/>	<hr style="border-top: 1px dashed black;"/>	<hr style="border-top: 1px dashed black;"/>
	81,643	153,387	3,696,436
NET LOSS BEFORE PROVISION FOR INCOME TAXES	<hr style="border-top: 1px dashed black;"/>	<hr style="border-top: 1px dashed black;"/>	<hr style="border-top: 1px dashed black;"/>
	(399,167)	(659,582)	(13,564,566)
PROVISION FOR INCOME TAXES	-	-	-
NET LOSS	<hr style="border-top: 1px dashed black;"/>	<hr style="border-top: 1px dashed black;"/>	<hr style="border-top: 1px dashed black;"/>
	\$ (399,167)	\$ (659,582)	\$ (13,564,566)
	<hr style="border-top: 1px dashed black;"/>	<hr style="border-top: 1px dashed black;"/>	<hr style="border-top: 1px dashed black;"/>
BASIC AND DILUTED LOSS PER COMMON SHARE	\$ (0.08)	\$ (0.19)	
	<hr style="border-top: 1px dashed black;"/>	<hr style="border-top: 1px dashed black;"/>	
WEIGHTED AVERAGE NUMBER OF COMMON SHARES			

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OUTSTANDING 5,234,072 3,417,029
===== =====

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

4

AETHLON MEDICAL, INC. AND SUBSIDIARIES
(A Development Stage Company)
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
For the Three Months Ended June 30, 2002 and
2001 and For the Period January 31, 1984
(Inception) Through June 30, 2002

(Unaudited)

	Three Months Ended June 30, 2002	Three Months Ended June 30, 2001	Ja (I
	-----	-----	-----
CASH FLOWS FROM OPERATING ACTIVITIES			
Net loss	\$ (399,167)	\$ (659,582)	\$ (13
Adjustments to reconcile net loss to net cash used in operating activities:			
Depreciation and amortization	40,879	82,349	
Gain on sale of furniture and equipment	-	-	
Interest and debt expenses related to warrants	(24,714)	92,728	2
Common stock, warrants and options issued for services	40,385	16,000	1
Beneficial conversion feature of convertible notes payable	80,000	-	
Impairment of goodwill	-	-	
Deferred compensation forgiven	-	-	
Changes in operating assets and liabilities:			
Prepaid expenses	5,863	7,245	
Other assets	-	-	
Accounts payable and accrued liabilities	78,362	37,763	1
Due to related parties	99,218	(64,923)	1
Net cash used in operating activities	(79,174)	(488,420)	(4
CASH FLOWS FROM INVESTING ACTIVITIES			
Acquisition of furniture and equipment	-	(30,804)	

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Acquisition of patents and patents pending	(10,986)	(19,597)
Proceeds from sale of furniture and equipment	-	-
Cash of acquired company	-	-
	-----	-----
Net cash used in investing activities	(10,986)	(50,401)

(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 Three Months Ended June 30, 2002 and
2001 and For the Period January 31, 1984
(Inception) Through June 30, 2002

(Unaudited)

	Three Months Ended June 30, 2002	Three Months Ended June 30, 2001	Jan (Inc T Ju
	-----	-----	-----
CASH FLOWS FROM FINANCING ACTIVITIES			
Proceeds from issuance of notes payable	\$ 105,000	\$ -	\$ 2
Principal payments in notes payable	(25,000)	-	
Net proceeds from issuance of common stock	-	689,264	2
	-----	-----	-----
Net cash provided by financing activities	80,000	689,264	4
	-----	-----	-----
NET (DECREASE) INCREASE IN CASH	(10,160)	150,443	
CASH - beginning of period	10,667	6,058	
	-----	-----	-----
CASH - end of period	\$ 507	\$ 156,501	\$
	=====	=====	=====

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

AETHLON MEDICAL, INC. AND SUBSIDIARIES
(A Development Stage Company)
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
June 30, 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 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 period ended June 30, 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

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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

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.

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 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.

Reclassifications

Certain reclassification have been made to the June 30, 2001 financial statement presentation to correspond to the June 30, 2002 format.

NOTE 3. DEBT-TO-EQUITY CONVERSION PROGRAM

In March 2002, the Company extended an offer to certain note holders and vendors to convert past due amounts into restricted common stock and warrants to purchase common stock of the Company. The offer entailed the conversion of liabilities at a conversion of one share and one-half of a warrant for every \$1.25 converted. The warrants have an exercise price of \$2.00 per share and expire three years from the date of issuance.

During the quarter ended June 30, 2002, note holders and vendors

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representing liabilities in the aggregate amounts of approximately \$238,000 converted their debt in exchange for 190,124 shares of Common Stock and 95,061 warrants to purchase common stock. Such warrants were valued using the

8

Black-Scholes option pricing model at approximately \$31,000 for the quarter ended June 30, 2002. The conversion rate exceeded the estimated market value of the Company's common stock.

NOTE 4. NOTES PAYABLE

At June 30, 2002, all outstanding promissory notes in the aggregate principal amount of \$472,500 were past due and in default.

On May 31, 2002, the Company issued notes to two investors in the total amount of \$25,000, bearing interest at 10% per annum. Principal and interest thereon became due June 9, 2002 and are now in default.

The Company is currently seeking other financing arrangements to retire all past due notes.

NOTE 5. CONVERTIBLE NOTES PAYABLE

On April 18, 2002, the Company issued a convertible note in the amount of \$50,000 to an investor bearing interest at 8% per annum, with principal and interest thereon due July 19, 2002. On May 3, 2002, the Company issued a convertible note in the amount of \$30,000 to an investor bearing interest a 10% per annum, with principal and interest thereon due June 2, 2002, and is now in default.

Both notes may be converted to common stock of the Company at any time at the option of the respective holder. The conversion price is the lower rate of \$1.25 per share or the offering terms set for any private equity offering initiated during the term of these notes. A beneficial conversion feature approximating \$80,000 was recorded during the quarter ended June 30, 2002.

The Company is seeking other financing arrangements to retire these notes, should the investors choose not to convert.

NOTE 6. 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 \$13.6 million for the period from January 31, 1984 (Inception) through June 30, 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 until such time that revenues achieve profitability levels.

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 operated cash flow to meet its obligations on a timely basis.

NOTE 7. 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 condition, 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 cash to fund registration expenses becomes available. The Company may incur additional charges in exchange for further waivers through the date of an effective registration statement.

Delinquent SEC Filing

The Company's March 31, 2002 Form 10-KSB did not contain certain disclosure items in its Management's Discussion and Analysis or Plan or Operation section including Executive Compensation, Security Ownership of Certain Beneficial Owners and Management and Certain Relationships and Related Transactions. Such filing delinquencies constitute securities laws non-compliance and, among other actions enforceable by the SEC, could result in de-listing of the Company's common stock from the 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 delinquencies are cured.

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

Results of Operations

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. Our main focus during fiscal 2002 was to further advance the HIV-Hemopurifier, AEMD-45.

We recorded a consolidated net loss of \$399,167 or \$(0.08) per share and

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\$659,582 or \$(0.19) per share for the quarters ended June 30, 2002 and 2001, respectively.

Consolidated operating expenses were \$317,524 for the three months ended June 30, 2002, versus \$506,195 for the comparable period in fiscal year 2001. This decrease in operating expenses is attributable to decreased professional fees, amortization and other expenses partially offset by higher personnel expenses.

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

Liquidity and Capital Resources

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 year end.

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 2002 and the first quarter of fiscal year 2003, we continued to issue promissory notes and convertible notes totaling \$283,000.

Additional funds in the aggregate amount of \$200,000 were generated in January and February 2002, through the exercise of an option to purchase common stock of the Company by a consultant.

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

Our operations to date have 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

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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.

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 Securities Exchange Act of 1934 ("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.

12

PART II

OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

None

ITEM 2. CHANGES IN SECURITIES

The Company issued 190,124 unregistered shares of common stock during the quarter ended June 30, 2002. Such stock, generally referred to as "Rule 144 stock," were not registered under the Securities Act of 1933, as amended, in reliance upon an exemption from its registration requirements.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

At August 19, 2002, various promissory and convertible notes payable in the aggregate principal amount of \$917,500 have reached maturity and

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

(b) Reports on Form 8-K filed during the quarter ended June 30, 2002.

None

13

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: August 19, 2002

By: /s/ JAMES A. JOYCE

James A. Joyce
Chairman, President and CEO

14