

FIRST NATIONAL CORP /VA/
 Form 4
 February 13, 2015

FORM 4

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION
 Washington, D.C. 20549**

OMB APPROVAL

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STATEMENT OF CHANGES IN BENEFICIAL OWNERSHIP OF SECURITIES

Filed pursuant to Section 16(a) of the Securities Exchange Act of 1934, Section 17(a) of the Public Utility Holding Company Act of 1935 or Section 30(h) of the Investment Company Act of 1940

(Print or Type Responses)

1. Name and Address of Reporting Person *
BEVERLEY JR MARSHALL J

2. Issuer Name and Ticker or Trading Symbol
FIRST NATIONAL CORP /VA/ [FXNC]

5. Relationship of Reporting Person(s) to Issuer

(Check all applicable)

(Last) (First) (Middle)
112 W KING STREET
 (Street)

3. Date of Earliest Transaction (Month/Day/Year)
02/11/2015

____ Director _____ 10% Owner
 Officer (give title below) _____ Other (specify below)
EVP / Senior Trust Officer

STRASBURG, VA 22657

(City) (State) (Zip)

4. If Amendment, Date Original Filed(Month/Day/Year)

6. Individual or Joint/Group Filing(Check Applicable Line)
 Form filed by One Reporting Person
 Form filed by More than One Reporting Person

Table I - Non-Derivative Securities Acquired, Disposed of, or Beneficially Owned

1. Title of Security (Instr. 3)	2. Transaction Date (Month/Day/Year)	2A. Deemed Execution Date, if any (Month/Day/Year)	3. Transaction Code (Instr. 8)	4. Securities Acquired (A) or Disposed of (D) (Instr. 3, 4 and 5)	5. Amount of Securities Beneficially Owned Following Reported Transaction(s) (Instr. 3 and 4)	6. Ownership Form: Direct (D) or Indirect (I) (Instr. 4)	7. Nature of Ownership (Instr. 4)	
			Code	V	Amount	(D)	Price	
Common Stock, \$1.25 par value	02/11/2015	02/11/2015	A	111	A	\$ 0	21,511	D

Reminder: Report on a separate line for each class of securities beneficially owned directly or indirectly.

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SEC 1474 (9-02)

Table II - Derivative Securities Acquired, Disposed of, or Beneficially Owned
(e.g., puts, calls, warrants, options, convertible securities)

1. Title of Derivative Security (Instr. 3)	2. Conversion or Exercise Price of Derivative Security	3. Transaction Date (Month/Day/Year)	3A. Deemed Execution Date, if any (Month/Day/Year)	4. Transaction Code (Instr. 8)	5. Number of Derivative Securities Acquired (A) or Disposed of (D) (Instr. 3, 4, and 5)	6. Date Exercisable and Expiration Date (Month/Day/Year)	7. Title and Amount of Underlying Securities (Instr. 3 and 4)	8. Price or Value of Derivative Security (Instr. 5)
Restricted Stock Units	(1)	02/11/2015		A	222	(2) (2)	Common Stock	222 \$ 0

Reporting Owners

Reporting Owner Name / Address	Relationships			
	Director	10% Owner	Officer	Other
BEVERLEY JR MARSHALL J 112 W KING STREET STRASBURG, VA 22657			EVP / Senior Trust Officer	

Signatures

Justin M. Hockman, by Power of Attorney
Date: 02/13/2015

**Signature of Reporting Person

Date

Explanation of Responses:

- * If the form is filed by more than one reporting person, see Instruction 4(b)(v).
- ** Intentional misstatements or omissions of facts constitute Federal Criminal Violations. See 18 U.S.C. 1001 and 15 U.S.C. 78ff(a).
- (1) Each restricted stock unit represents a contingent right to receive one share of FXNC common stock.
- (2) The restricted stock units vest in two equal annual installments beginning February 11, 2016.

Note: File three copies of this Form, one of which must be manually signed. If space is insufficient, see Instruction 6 for procedure. Potential persons who are to respond to the collection of information contained in this form are not required to respond unless the form displays a currently valid OMB number. TYLE="text-align: left"> 0.11 0.06 Second Quarter 0.13 0.07 First Quarter 0.18 0.05

There were approximately 194 record holders of our common stock at December 31, 2014. The number of registered stockholders includes any beneficial owners of common shares held in street name.

We have not declared any cash dividends on our common stock since inception and do not anticipate any in the future. Any future determination to pay cash dividends will be at the discretion of our Board of Directors, and will be dependent upon our financial condition, results of operations, capital requirements and other factors our Board of Directors may deem relevant at that time.

The transfer agent and registrar for our common stock is Computershare Investor Services, located at 350 Indiana Street, Suite 800, Golden, Colorado 80401.

Equity Compensation Plans

Summary equity compensation plan data

The following table sets forth information, as of March 31, 2014, about our equity compensation plans (including the potential effect of debt instruments convertible into common stock) in effect as of that date:

Plan category	(a) Number of securities to be issued upon exercise of outstanding options, warrants and rights (1)(2)	(b) Weighted-average exercise price of outstanding options, warrants and rights	(c) Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))
Equity compensation plans approved by security holders	–	\$ –	490,000
Equity compensation plans not approved by security holders (1)(3)(4)	26,133,407	\$ 0.25	2,445,626

Explanation of Responses:

Totals	26,133,407	\$ 0.25	2,935,626
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(1) The description of the material terms of non-plan issuances of equity instruments is discussed in Note 6 to the accompanying consolidated financial statements.

(2) Net of equity instruments forfeited, exercised or expired.

(3) On June 8, 2009, our Board of Directors approved the grant to Mr. James A. Joyce, our Chief Executive Officer, of 4,000,000 shares of restricted common stock. The market price of our stock on the grant date was \$0.24 per share and the shares vested in equal installments over a thirty-six-month period that commenced on June 30, 2010.

(4) On March 31, 2014 we had 2,445,626 shares available under our 2010 Stock Incentive Plan.

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2000 Stock Option Plan

Our 2000 Stock Option Plan provides for the grant of incentive stock options to our full-time employees (who may also be directors) and nonstatutory stock options to non-employee directors, consultants, customers, vendors or providers of significant services. The exercise price of any incentive stock option may not be less than the fair market value of the common stock on the date of grant or, in the case of an optionee who owns more than 10% of the total combined voting power of all classes of our outstanding stock, not be less than 110% of the fair market value on the date of grant. The exercise price, in the case of any nonstatutory stock option, must not be less than 75% of the fair market value of the common stock on the date of grant. The amount reserved under the 2000 Stock Option Plan is 500,000 options.

At March 31, 2014, all of the grants previously made under the 200 Stock Option Plan had expired and 10,000 restricted shares had been issued under the plan, with 490,000 available for future issuance.

2003 Consultant Stock Plan

Our 2003 Consultant Stock Plan advances our interests by helping us obtain and retain the services of persons providing consulting services upon whose judgment, initiative, efforts and/or services we are substantially dependent, by offering to or providing those persons with incentives or inducements affording such persons an opportunity to become owners of our capital stock. Consultants or advisors are eligible to receive grants under the plan program only if they are natural persons providing bona fide consulting services to us, with the exception of any services they may render in connection with the offer and sale of our securities in a capital-raising transaction, or which may directly or indirectly promote or maintain a market for our securities. The plan provides for the grant of common stock. No awards may be issued after the ten-year anniversary of the date we adopted the plan, the termination date for the plan. We have periodically amended the plan to increase the number of shares available for issuance under the plan with the approval of our Board of Directors.

We filed registration statements on Form S-8 with the Securities and Exchange Commission to register under the Securities Act of 1933, as amended, the common shares issuable under this plan as follows:

<u>Date of Filing</u>	<u>Number of Shares Registered</u>
March 29, 2004	1,000,000
August 29, 2005	2,000,000
August 9, 2007	2,000,000
July 10, 2009	1,000,000
February 17, 2010	1,500,000

We discontinued using this plan in October 2012.

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2010 Stock Incentive Plan

In August 2010, we adopted the 2010 Stock Incentive Plan, which provides incentives to attract, retain and motivate employees and directors whose present and potential contributions are important to our success by offering them an opportunity to participate in our future performance through awards of options, the right to purchase common stock, stock bonuses and stock appreciation rights and other awards. A total of 3,500,000 common shares were initially reserved for issuance under the 2010 Stock Incentive Plan.

In August 2010, we filed a registration statement on Form S-8 for the purpose of registering 3,500,000 common shares issuable under this plan under the Securities Act of 1933, as amended, and in July 2012, we filed a registration statement on Form S-8 for the purpose of registering 5,000,000 common shares issuable under this plan under the Securities Act of 1933, as amended.

At March 31, 2014, we had 2,445,626 shares available under this plan.

2012 Directors Compensation Program

In July 2012, our Board of Directors approved a board compensation program that modifies and supersedes the 2005 Directors Compensation Program, which was previously in effect. Under the 2012 program, in which only non-employee directors may participate, an eligible director will receive a grant of \$35,000 worth of ten year options to acquire shares of common stock, with such grant being valued at the exercise price based on the average of the closing bid prices of the common stock for the five trading days preceding the first day of the fiscal year. In addition, under this new program, eligible directors will receive cash compensation equal to \$500 for each committee meeting attended and \$1,000 for each formal board meeting attended.

In the fiscal year ended March 31, 2013, our Board of Directors granted ten-year options to acquire an aggregate of 1,667,105 shares of our common stock, all with an exercise price of \$0.076 per share, to our four outside directors under the new 2012 program.

In the fiscal year ended March 31, 2014, our Board of Directors granted ten-year options to acquire an aggregate of 1,595,536 shares of our common stock, all with an exercise price of \$0.082 per share, to our five outside directors under the new 2012 program.

At March 31, 2014 we had issued 1,337,825 options under the old 2005 program to outside directors and 3,965,450 options to employee-directors, 514,550 outside directors' options had been forfeited, 250,000 outside directors' options had been exercised and 3,671,550 options remained outstanding.

On June 6, 2014, our Board of Directors approved certain changes to the 2012 program. Under this new program, a new eligible director will receive an initial grant of \$50,000 worth of options to acquire shares of common stock, with such grant being valued at the exercise price based on the average of the closing bid prices of the common stock for the five trading days preceding the first day of the fiscal year. These options will have a term of ten years and will vest 1/3 upon grant and 1/3 upon each of the first two anniversaries of the date of grant. In addition, at the beginning of each fiscal year, each existing director eligible to participate in the modified new 2012 program also will receive a grant of \$35,000 worth of options valued at the exercise price based on the average of the closing bid prices of the common stock for the five trading days preceding the first day of the fiscal year. Such options will vest on the first anniversary of the date of grant. In lieu of per meeting fees, eligible directors will receive an annual board retainer fee of \$30,000. The modified new 2012 program also provides for the following annual retainer fees: Audit Committee Chair - \$5,000, Compensation Committee chair - \$5,000, Audit Committee member - \$4,000, Compensation Committee member - \$4,000 and lead independent director - \$15,000.

Stand-alone grants

From time to time our Board of Directors grants restricted stock or common share purchase options or warrants to selected directors, officers, employees and consultants as equity compensation to such persons on a stand-alone basis outside of any of our formal stock plans. The terms of these grants are individually negotiated.

On June 8, 2009, our Board of Directors approved the grant to Mr. Joyce of 4,000,000 shares of restricted common stock at a price per share of \$0.24, the vesting and issuance of which occurred in equal installments over a thirty-six-month period that commenced on June 30, 2010.

As of March 31, 2014, we had issued 22,568,158 options (of which 3,368,942 have been exercised or cancelled) and authorized the issuance of 4,000,000 shares of restricted stock outside of the 2005 Directors Compensation Plan, the 2012 Directors Compensation Plan, the 2000 Stock Option Plan, the 2003 Consultant Stock Plan and the 2010 Incentive Stock Plan.

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

The following discussion and analysis should be read in conjunction with the consolidated Financial Statements and Notes thereto appearing elsewhere in this prospectus.

Overview

We are a medical device company focused on creating innovative devices that address unmet medical needs in cancer, infectious disease and other life-threatening conditions. At the core of our developments is the Aethlon ADAPT system, a medical device platform that converges single or multiple affinity drug agents with advanced plasma membrane technology to create therapeutic filtration devices that selectively remove harmful particles from the entire circulatory system without loss of essential blood components.

In June 2013, the U.S. Food and Drug Administration approved our investigational device exemption application to initiate a ten-patient human clinical trial in one location in the United States to treat dialysis patients who are infected with the Hepatitis-C virus. The principal investigator of that clinical trial recently began recruiting patients. Successful outcomes of that human trial as well as at least one follow-on human trial will be required by the U.S. Food and Drug Administration in order to commercialize our products in the U.S. The regulatory agencies of certain foreign countries where we intend to sell this device will also require one or more human clinical trials.

Some of our patents may expire before we receive U.S. Food and Drug Administration approval to market our products in the United States or we receive approval to market our products in a foreign country. However, we believe that certain patent applications and/or other patents issued more recently will help protect the proprietary nature of the Hemopurifier treatment technology.

In October 2013, our majority-owned subsidiary, Exosome Sciences, Inc., commenced operations with a focus on advancing exosome-based strategies to diagnose and monitor the progression of cancer, infectious disease and other life-threatening conditions.

Fiscal Years Ended March 31, 2014 and 2013

Results of Operations

Explanation of Responses:

Revenues

We recorded government contract revenue in the fiscal years ended March 31, 2014 and 2013. This revenue arose from work performed under our government contract with the Defense Advanced Research Projects Agency and our subcontract with Battelle Memorial Institute as follows:

	Fiscal Year Ended 3/31/14	Fiscal year Ended 3/31/13	Change in Dollars
Defense Advanced Research Projects Agency contract	\$1,466,482	\$1,230,004	\$236,478
Battelle Memorial Institute subcontract	157,287	–	157,287
Total government contract revenue	\$1,623,769	\$1,230,004	\$393,765

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Defense Advanced Research Projects Agency Contract

We entered into a contract with the Defense Advanced Research Projects Agency on September 30, 2011. Under the Defense Advanced Research Projects Agency award, we have been engaged to develop a therapeutic device to reduce the incidence of sepsis, a fatal bloodstream infection that often results in the death of combat-injured soldiers. The award from the Defense Advanced Research Projects Agency was a fixed-price contract with potential total payments to us of \$6,794,389 over the course of five years. Fixed price contracts require the achievement of multiple, incremental milestones to receive the full award during each year of the contract. Under the terms of the contract, we will perform certain incremental work towards the achievement of specific milestones against which we will invoice the government for fixed payment amounts.

Originally, only the base year (year one contract) was effective for the parties; however, the Defense Advanced Research Projects Agency subsequently exercised the option on the second, third and fourth years of the contract. The Defense Advanced Research Projects Agency has the option to enter into the contract for year five. The milestones are comprised of planning, engineering and clinical targets, the achievement of which in some cases will require the participation and contribution of third party participants under the contract. There can be no assurance that we alone, or with third party participants, will meet such milestones to the satisfaction of the government and in compliance with the terms of the contract or that we will be paid the full amount of the contract revenues during any year of the contract term. We commenced work under the contract in October 2011.

Due to budget restrictions within the Department of Defense, on February 10, 2014, the Defense Advanced Research Projects Agency reduced the scope of our contract in years three through five of the contract. The reduction in scope focused our research on exosomes, viruses and blood processing instrumentation. This scope reduction will reduce the possible payments under the contract by \$858,491 over years three through five.

As a result of achieving eight milestones in the fiscal year ended March 31, 2014, we reported \$1,466,482 in contract revenue for that fiscal year and as a result of achieving six milestones in the fiscal year ended March 31, 2013, we reported \$1,230,004 in contract revenue for that fiscal year.

As of March 31, 2014, we have invoiced for twenty milestone payments under the Defense Advanced Research Projects Agency contract totaling \$4,054,675.

Battelle Memorial Institute Subcontract

We entered into a subcontract agreement with Battelle Memorial Institute in March 2013. Battelle Memorial Institute was chosen by the Defense Advanced Research Projects Agency to be the prime contractor on the systems integration

portion of the original Defense Advanced Research Projects Agency contract and we are one of several subcontractors on that systems integration project. The Battelle Memorial Institute subcontract is under a time and materials basis and we began generating revenues under the subcontract in the three months ended September 30, 2013. Our expected future revenue from the subcontract will be at the discretion of Battelle Memorial Institute. The Battelle Memorial Institute subcontract is our first cost-reimbursable contract.

Our revenue under this contract is a function of cost reimbursement plus an overhead mark-up for hours devoted to the project by specific employees (with specific hourly rates for those employees), for travel expenses related to the project, for any equipment purchased for the project and for the cost of any consultants hired by us to perform work on the project. Each payment will require approval by the program manager at Battelle Memorial Institute.

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Operating Expenses

Consolidated operating expenses were \$4,679,697 for the fiscal year ended March 31, 2014 compared to \$4,805,358 in the fiscal year ended March 31, 2013, a decrease of \$125,661. The net decrease of \$125,661 was due to a decrease in professional fees of \$370,873, which was partially offset by an increase in general and administrative expense of \$185,007 and an increase in payroll and related expenses of \$60,205.

The \$370,873 decrease in our professional fees primarily arose from a decrease in Defense Advanced Research Projects Agency-related professional fees of \$223,930 due to decreased use of consultants on subtask 1 of the project and a decrease in non-Defense Advanced Research Projects Agency-related professional fees of \$187,922. Those decreases were partially offset by \$40,979 in professional fees at our Exosome Sciences, Inc. subsidiary. The decrease in non-Defense Advanced Research Projects Agency-related professional fees was primarily due to decreased activity in our Hepatitis-C trial in India.

The \$185,007 increase in general and administrative expenses primarily arose from \$130,367 in general and administrative expenses from the recently launched operations at our majority-owned Exosome Sciences, Inc. subsidiary. We also had a \$65,862 increase in general and administrative expenses related to our government contracts, which was partially offset by a \$11,222 decrease in our non- Exosome Sciences, Inc., non-Defense Advanced Research Projects Agency-related general and administrative expenses.

The \$60,205 increase in payroll and related expenses was principally driven by \$232,719 in payroll and related expenses from the recently launched operations at our majority-owned Exosome Sciences, Inc. subsidiary. That increase was partially offset by a \$157,327 reduction in our stock-based compensation.

Other Expense

In the fiscal year ended March 31, 2014, we recognized other expenses of \$10,383,034 compared to \$1,316,686 of other expense in the fiscal year ended March 31, 2013. The following table breaks out the various components of our other expense over the fiscal years ended March 31, 2014 and 2013:

	Components of Other Expense in Fiscal Year Ended		
	March 31, 2014	March 31, 2013	Change
Loss on debt conversion and on settlement of accrued interest and damages	\$40,257	\$139,839	\$(99,582)

Explanation of Responses:

Change in fair value of derivative liability	8,547,015	44,705	8,502,310
Interest and other debt expenses	1,287,221	1,132,314	154,907
Loss on litigation settlement	583,601	–	583,601
Other	(75,060)	(172)	(74,888)
Total other expense	\$10,383,034	\$1,316,686	\$9,066,348

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We recorded a loss on debt conversion and on settlement of accrued interest and damages of \$40,257 and \$139,839 in the fiscal years ended March 31, 2014 and 2013, respectively. In the both fiscal years, those losses arose from the conversion to equity of principal and accrued interest on certain notes payable.

Both periods include changes in the fair value of derivative liability. For the fiscal year ended March 31, 2014, the change in the estimated fair value of derivative liability was a loss of \$8,547,015 and for the fiscal year ended March 31, 2013, the change in the estimated fair value of derivative liability was a loss of \$44,705.

We also recorded litigation settlement expense of \$583,601 in the fiscal year ended March 31, 2014.

Other income included a gain of \$75,000 related to the extinguishment of accrued damages as a result of the litigation settlement in the fiscal year ended March 31, 2014 as well as interest income in both fiscal years.

Our interest and other debt expense increased by \$154,907 from the fiscal year ended March 31, 2013 to the fiscal year ended March 31, 2014. The following table breaks out the various components of our interest expense over the fiscal years ended March 31, 2014 and 2013:

	Components of Interest Expense and Other Debt		
	Expenses in Fiscal Year Ended		
	March 31, 2014	March 31, 2013	Change
Interest expense	\$425,725	\$526,110	\$(100,385)
Amortization of deferred financing costs	863	127,200	(126,337)
Amortization of note discounts	4,284	467,158	(462,874)
Note restructuring expense	856,349	–	856,349
Non-cash interest expense	–	11,846	(11,846)
Total interest expense	\$1,287,221	\$1,132,314	\$154,907

As a result of the above factors, our net loss before noncontrolling interests increased from \$(4,892,040) for the fiscal year ended March 31, 2013 to \$(13,438,962) for the fiscal year ended March 31, 2014.

Liquidity and Capital Resources

At March 31, 2014, we had a cash balance of \$1,250,279 and a working capital deficit of \$14,169,471. This compares to a cash balance of \$125,274 and a working capital deficit of \$9,276,618 at March 31, 2013. Between April 1, 2014 and July 9, 2014, we raised aggregate proceeds of \$320,800 through private equity transactions and collected \$135,376 under our Defense Advanced Research Projects Agency contract and Battelle Memorial Institute subcontract. Significant additional financing must be obtained in order to provide a sufficient source of operating capital and to allow the Company to continue to operate as a going concern. In addition, we will need to raise capital to complete the recently approved human clinical trial in the U.S. During the period after March 31, 2014, we raised capital to support our operations. See the discussions in the sections below entitled “Three and Six-Month Periods Ended September 30, 2014 and 2013” and “Material Changes During the Period September 30, 2014 to December 31, 2014.”

We do not expect revenue from operations will be sufficient to satisfy our funding requirements in the near term, and accordingly, our ability to continue operations and 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. Future capital requirements will depend upon many factors, including progress with pre-clinical testing and clinical trials, the number and breadth of our clinical 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, as well as 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.

Cash Flows

Cash flows from operating, investing and financing activities, as reflected in the accompanying Consolidated Statements of Cash Flows, are summarized as follows (in thousands):

	(In thousands)	
	For the year ended	
	March 31, 2014	March 31, 2013
Cash (used in) provided by:		
Operating activities	\$(2,139)	\$(2,099)
Investing activities	(96)	–
Financing activities	3,360	2,080
Net increase (decrease) in cash	\$1,125	\$(19)

Net Cash from Operating Activities.

We used cash in our operating activities due to our losses from operations. Net cash used in operating activities was approximately \$2,139,000 in fiscal 2014 compared to net cash used in operating activities of approximately \$2,099,000 in fiscal 2013, an increase of \$40,000. The \$40,000 increase was primarily due to changes in our operating assets and liabilities.

Net Cash from Investing Activities.

During the fiscal year ended March 31, 2014, we used approximately \$96,000 in cash for purchases of equipment. During the fiscal year ended March 31, 2013, we did not purchase any equipment or have any other investing activities.

Net Cash from Financing Activities.

Net cash generated from financing activities increased from approximately \$2,080,000 in the fiscal year ended March 31, 2013 to approximately \$3,360,000 in the fiscal year ended March 31, 2014. Included in net cash provided by financing activities in fiscal 2014 were approximately \$3,177,000 from the issuance of common stock and \$400,000 from the issuance of notes payable, which was partially offset by approximately \$217,000 in repayments of notes payable in cash. In fiscal 2013, we received approximately \$2,110,000 from the issuance of common stock, which was partially offset by approximately \$30,000 in repayments of notes payable and related accrued interest in cash.

Convertible Notes Payable and Warrants

Amended and Restated 12% Series A Convertible Notes

In June 2010, we entered into Amended and Restated 12% Series A Convertible Promissory Notes, in the principal amount of \$900,000, with the holders of certain promissory notes previously issued by us. These notes matured on December 31, 2010. In connection with the amendments we paid \$54,001 of accrued and default interest through the date of the restructuring, liquidated damages of \$205,000 and \$54,003 of prepaid interest through the expiration date in the aggregate amount of \$313,004 through the issuance of units at a fixed rate of \$0.20 per unit. Each unit consists of one share of our common stock and one common stock purchase warrant to purchase one share of our common stock at a fixed exercise price of \$0.20 per share exercisable until February 2016. We also increased the annual interest rate from ten percent to twelve percent. We also agreed to change the exercise prices on all of the warrants held by the noteholders to \$0.20 per share, to change certain formerly contingent warrants to non-contingent warrants and to extend the expiration date of their warrants to February 2016. As of December 31, 2013 the notes were in default. We accrued interest at the revised default rate of 20% following December 31, 2010.

On June 24, 2014, we entered into an agreement with the Ellen R. Weiner Family Revocable Trust, a holder of one of the notes to convert past due combined principal and interest balance of \$1,003,200 into an aggregate of 23,318,254 restricted shares of our common stock and five-year warrants to acquire up to 6,809,524 shares of our common stock at an exercise price of \$.042 per share and 397,222 shares of our common stock at an exercise price of \$.108 per share. In connection with these changes, the trust agreed to waive the anti-dilution price protection in the warrants.

In exchange for the trust's conversion in full of the note and accrued interest and for the waivers of anti-dilution price protection in the previously issued warrants, we also issued to the trust 75,000 restricted shares of common stock as a service fee, changed the exercise price of all of the previously issued warrants to \$.042 per share and extended the expiration date of all of the previously issued warrants to July 1, 2018.

On July 8, 2014, we entered into an agreement with the Estate of Allan Bird, a holder of a one of the notes that was in default. In the agreement, the estate agreed to extend the expiration date of the note to April 1, 2016, and to convert approximately \$116,970 of accrued interest into an aggregate of 2,591,846 restricted shares of our common stock. The estate received five-year warrants to acquire 2,321,429 shares of our common stock at an exercise price of \$.042 per share and 135,417 shares of our common stock at an exercise price of \$.108.

We also issued to the estate 25,000 restricted shares of common stock as a service fee, changed the exercise price of all of the previously issued warrants to \$.042 per share and extended the expiration date of all of the previously issued warrants to July 1, 2018.

December 2006 10% Convertible Notes

In January 2014, we paid off the remaining December 2006 10% Note and the related accrued interest balance with a cash payment of \$35,055. That payment represented the sum of the \$17,000 principal balance and \$18,055 of accrued interest.

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2008 10% Convertible Notes

One 2008 10% Convertible Note in the amount of \$25,000, which matured in January 2010 remained outstanding at March 31, 2014. On September 17, 2014, we issued the holder 478,188 shares of restricted common stock and warrants to acquire up to 239,094 shares of common stock at an exercise price of \$0.14 per share upon conversion of the entire outstanding principal amount of \$25,000 and accrued interest of \$20,906.

October and November 2009 10% Convertible Notes

In October and November 2009, we raised \$430,000 from the sale to accredited investors of 10% convertible notes. The notes matured at various dates between April 2011 and May 2011 and are convertible into our common stock at a fixed conversion price of \$0.25 per share prior to maturity. The investors also received matching three year warrants to purchase unregistered shares of our common stock at a price of \$0.25 per share. We measured the fair value of the warrants and the beneficial conversion feature of the notes and recorded a 100% discount against the principal of the notes. We are amortizing this discount using the effective interest method over the term of the notes.

Deferred financing costs of \$20,250 incurred in connection with this financing were issued in the form of a convertible note with warrants on the same terms as those received by the investors. We capitalized the \$20,250 of deferred financing costs and amortized them over the term of the notes using the effective interest method.

In July 2012, we issued 461,409 shares of common stock to the holder of the one of the notes in the principal amount of \$25,000 in exchange for the value of the principal and related accrued interest of \$8,000 under the same terms that we used to sell units consisting of one share of common stock and one-half of a stock purchase warrant on June 29, 2012. The 461,409 share issuance was priced based on 80% of the trailing five day average before issuance to be consistent with the equity unit structure. As part of that structure, the noteholder also received seven year warrants to purchase 230,705 share of common stock at a price of \$0.107 per share. The \$16,149 value of the warrant was calculated using the binomial lattice valuation methodology. We recorded a loss on conversion of \$45,796 on the conversions in the quarter ended September 30, 2012.

The following table shows the conversions into principal of the October and November 2009 Convertible Notes by fiscal year:

Activity in October and November 2009 Convertible Notes

Initial principal balance, including \$250,000 of deferred financing costs	\$450,250
Conversions during the fiscal year ended March 31, 2010	(70,000)
Conversions during the fiscal year ended March 31, 2011	(175,000)

Explanation of Responses:

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Conversions during the fiscal year ended March 31, 2012	(130,250)
Conversions during the fiscal year ended March 31, 2013	(25,000)
Conversions during the fiscal year ended March 31, 2014	–
Balance as of March 31, 2014	\$50,000

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In September 2013, we agreed to extend the expiration date of certain warrants of one of the note holders by two years in exchange for the extension to April 22, 2015 of the maturity date of a \$50,000 note previously issued to the holder. Management assessed the change in the value of the note and related warrants before and after that extension and determined that the change in value related to the change in terms was not significant.

April 2010 10% Convertible Note

In April 2010, we raised \$75,000 from the sale to an accredited investor of a 10% convertible note. The convertible note matured in October 2011 and is convertible into our common stock at a fixed conversion price of \$0.25 per share prior to maturity. The investor also received three year warrants to purchase 300,000 unregistered shares of our common stock at a price of \$0.25 per share.

We measured the fair value of the warrants and the beneficial conversion feature of the notes and recorded a 100% discount against the principal of the notes. We amortized this discount using the effective interest method over the term of the note. As of March 31, 2014, there have not been any conversions of the note.

In September 2013, we agreed to extend the expiration date of certain warrants of the note holder by two years in exchange for the extension of the maturity date of the \$75,000 note to October 21, 2015. Management assessed the change in the value of the notes and related warrants before and after that extension and determined that the change in value related to the change in terms was not significant.

September 2010 10% Convertible Notes

On September 3, 2010, we entered into a subscription agreement with three accredited investors providing for the issuance and sale of convertible promissory notes and corresponding warrants in the aggregate principal amount of \$1,430,000. The closing resulted in the issuance and sale of (i) convertible promissory notes in the aggregate principal amount of \$743,600, (ii) five-year warrants to purchase an aggregate of 3,718,000 shares of our common stock at an exercise price of \$0.31125 per share, and (iii) five-year warrants to purchase an aggregate of 3,718,000 shares of our common stock at an exercise price of \$0.43575 per share. The convertible promissory notes bear interest compounded monthly at the annual rate of ten percent (10%) and matured on September 3, 2011. The aggregate gross cash proceeds were \$650,000, the balance of the principal amount representing a due diligence fee and an original issuance discount. The convertible promissory notes are convertible at the option of the holders into shares of our common stock at a price per share equal to eighty percent (80%) of the average of the three lowest closing bid prices of the common stock as reported by Bloomberg L.P. for the principal market on which the common stock trades or is quoted for the ten (10) trading days preceding the proposed conversion date. Subject to adjustment as described in the notes, the conversion price may not be more than \$0.30 nor less than \$0.20.

On March 31, 2014, we amended these notes to extend the maturity date to April 1, 2016, which permits us to classify them as long-term liabilities. The non-default interest rate for all of the notes was set at twelve percent per annum. We also agreed to increase the outstanding principal amount of the notes by 12% from a total of \$693,260 to a total of \$776,451.

During the period from October 2011 to February 2014, the investors converted, at conversion prices between \$.0546 and \$.07 per share, portions of principal and interest outstanding under these notes and certain other convertible promissory notes previously issued to them by us. Certain anti-dilution provisions applicable to such notes should have resulted in such conversions being effected at a conversion price of \$.042 per share. Accordingly, we issued to the investors an additional 4,507,105 shares of our common stock, which represents the additional shares of common stock that would have been issued to the investors had such conversions been effected at \$.042 per share.

The amendments also set the conversion price of the notes, as well as the exercise price at which shares of our common stock can be purchased under the warrants, at \$.042 per share. By virtue of the amendments, the expiration dates of the warrants also were extended from dates between September 3, 2015 and September 23, 2016 to January 1, 2017.

The following table shows the activity in these notes by fiscal year:

Activity in September 2010 10% Convertible Notes

Initial principal balance	\$ 743,600
Conversions during the fiscal year ended March 31, 2012	(405,500)
Conversions during the fiscal year ended March 31, 2013	(30,000)
Conversions during the fiscal year ended March 31, 2014	(25,000)
Increase in principal balance due to 12% extension fee	33,972
Balance as of March 31, 2014	\$ 317,072

April 2011 10% Convertible Notes

In April 2011, we entered into a subscription agreement with two accredited investors providing for the issuance and sale of convertible promissory notes and corresponding warrants which resulted in the issuance and sale by us of (i) convertible promissory notes in the aggregate principal amount of \$385,000, (ii) five-year warrants to purchase an aggregate of 4,004,000 shares of our common stock at an exercise price of \$0.125 per share, and (iii) five-year warrants to purchase an aggregate of 4,004,000 shares of our common stock at an exercise price of \$0.175 per share. The convertible promissory notes bear interest compounded monthly at the annual rate of ten percent and matured on April 1, 2012. The aggregate gross cash proceeds to us were \$350,000, the balance of the principal amount representing a due diligence fee and an original issuance discount. The convertible promissory notes were convertible at the option of the holders into shares of our common stock at a price per share equal to eighty percent (80%) of the average of the three lowest closing bid prices of the common stock as reported by Bloomberg L.P. for the principal market on which the common stock trades or is quoted for the ten (10) trading days preceding the proposed conversion date. Subject to adjustment as described in the notes, the conversion price may not be more than \$0.20 nor less than \$0.10. There are no registration requirements with respect to the shares of common stock underlying the notes or the warrants.

In addition, we issued (i) five-year warrants to purchase an aggregate of 812,500 shares of our common stock at an exercise price of \$0.125 per share, and (ii) five-year warrants to purchase an aggregate of 812,500 shares of our common stock at an exercise price of \$0.175 per share to the purchasers. These warrants were issued as an anti-dilution adjustment under certain common stock purchase warrants held by the purchasers that were acquired from us in September 2010.

On March 31, 2014, we entered into amendments with three accredited investors with respect to notes and warrants previously issued by us on various dates between December 5, 2007 and September 23, 2011, including these notes.

Prior to the amendments, the notes were past maturity and were in default, resulting in the accrual of interest at the applicable default interest rate. The amendments extended the maturity date of each of the notes to April 1, 2016 and provided for a non-default interest rate for all of the notes at twelve percent per annum, which represents a reduction from the default interest rates of fifteen percent at which interest had been accruing. By entering into the amendments, we also agreed to increase the outstanding principal amount of the notes by 12% from a total of \$693,260 to a total of \$776,451.

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During the period from October 2011 to February 2014, the investors had converted, at conversion prices between \$.0546 and \$.07 per share, portions of principal and interest outstanding under the Notes and certain other convertible promissory notes previously issued to them by us. Certain anti-dilution provisions applicable to such notes should have resulted in such conversions being effected at a conversion price of \$.042 per share. Thus, we issued to the investors an aggregate of 4,507,105 shares of our common stock, which represents the additional shares of common stock that would have been issued to the Investors had such conversions been effected at \$.042 per share.

The amendments also set the conversion price of the notes, as well as the exercise price at which shares of our common stock can be purchased under the warrants, at \$.042 per share. In addition, the warrants also were extended from dates between September 3, 2015 and September 23, 2016 to January 1, 2017.

As of March 31, 2014, there have not been any conversions of these notes and the 12% extension fee noted above increased the principal balance by \$48,048 to a principal balance of \$ 448,448.

July and August 2011 10% Convertible Notes

During the three months ended September 30, 2011, we raised \$357,656 in 10% convertible notes. Those notes had a fixed conversion price of \$0.09 per share and carried an interest rate of 10%. The convertible notes matured in July and August 2012. We also issued those investors five year warrants to purchase 3,973,957 shares of common stock at \$0.125 per share.

We measured the fair value of the warrants and the beneficial conversion feature of the notes and recorded a \$257,926 discount against the principal of the notes. We amortized this discount using the effective interest method over the term of the note. As of September 30, 2013, there were no conversions of the notes, which were extended to July 16, 2014.

Effective July 14, 2012, holders of three notes totaling \$100,000 agreed to extend the expiration date of their notes to July 13, 2013. Subsequent to June 30, 2013, the holders of the three notes agreed to extend their notes to July 16, 2014. As part of the extension, we agreed to capitalize accrued interest of \$20,027 into the principal balance. Effective March 31, 2014, the holders of the three notes converted all of their principal and accrued interest into 1,438,700 shares of our common stock at the contractual conversion price of \$0.09 per share.

At March 31, 2014, the outstanding principal balance was \$257,655, all of which was in default. We recorded interest at the default interest rate of 15%.

September 2011 Convertible Notes

On September 23, 2011, we entered into a subscription agreement with two accredited investors providing for the issuance and sale of convertible promissory notes and corresponding warrants in the aggregate principal amount of \$253,760. The warrants carried a five-year term to purchase an aggregate of 3,625,143 shares of our common stock at an exercise price of \$0.10 per share. The convertible promissory notes do not bear an interest rate and matured on September 23, 2012. The aggregate net cash proceeds to us were \$175,000, the balance of the principal amount representing a due diligence fee and an original issuance discount. The convertible promissory notes are convertible at the option of the holders into shares of our common stock at a price per share equal to \$0.07. Subject to adjustments as described in the notes, the conversion price may not be more than \$0.07.

We measured the fair value of the warrants and the beneficial conversion feature of the notes and recorded a \$168,804 discount against the principal of the notes. We amortized this discount using the effective interest method over the term of the note.

On March 31, 2014, we entered into separate amendments with three accredited investors who own certain convertible promissory notes and warrants previously issued by us on various dates between December 5, 2007 and September 23, 2011, including these notes.

The amendments extended the maturity date of each of the notes to April 1, 2016, and the non-default interest rate for all of the notes was set at 12% per annum, which represents a reduction from the default interest rates of 15% at which interest had been accruing. By entering into the amendments, we also agreed to increase the outstanding principal amount of the notes by 12% from a total of \$693,260 to a total of \$776,451.

During the period from October 2011 to February 2014, the investors had converted, at conversion prices between \$.0546 and \$.07 per share, portions of principal and interest outstanding under the notes and certain other convertible promissory notes previously issued to them by us. Certain anti-dilution provisions applicable to such notes should have resulted in such conversions being effected at a conversion price of \$.042 per share. Accordingly, pursuant to the amendments, we issued to the investors an aggregate of 4,507,105 shares of our common stock, which represents the additional shares of common stock that would have been issued to the Investors had such conversions been effected at \$.042 per share.

The amendments also set the conversion price of the notes, as well as the exercise price at which shares of our common stock can be purchased under the warrants, at \$.042 per share. Additionally, under the amendments, the expiration dates of the warrants also were extended from dates between September 3, 2015 and September 23, 2016 to January 1, 2017.

The following table shows the conversions into principal of these notes by fiscal year:

Activity in September 2011 Convertible Notes

Initial principal balance	\$253,760
Conversions during the fiscal year ended March 31, 2012	(15,000)
Conversions during the fiscal year ended March 31, 2013	(60,000)
Conversions during the fiscal year ended March 31, 2014	(169,000)
Increase in principal balance due to extension fee	1,171
Balance as of March 31, 2014	\$ 10,931

Law Firm Note Number 1

Explanation of Responses:

On March 22, 2012, we entered into a promissory note with our corporate law firm for the amount of \$75,000, which represented the majority of the amount we then owed to that firm. The promissory note originally had a maturity date of December 31, 2012 and bears interest at five percent per annum. The note is convertible at the option of the holder into shares of our common stock at a 10% discount to the market price of the common stock on the date prior to conversion with a floor price on such conversions of \$0.08 per share. During the quarter ended June 30, 2013, the parties agreed to extend the maturity date of the note to October 1, 2013 and subsequent to September 30, 2013, the expiration date of this note was again extended to October 1, 2014. On November 7, 2014, we paid in full the outstanding principal balance and related accrued interest with a cash payment of \$50,000 and an issuance of 170,020 shares of common stock upon conversion at a conversion price of \$0.21 per share.

Law Firm Note Number 2

On June 4, 2013, we entered into a promissory note with our corporate law firm for the amount of \$47,000, which represented approximately 50% of the amount we owed to that firm for services in 2012. The promissory note had a maturity date of October 1, 2014 and bears interest at five percent per annum. The note was convertible at the option of the holder into shares of our common stock at a 10% discount to the market price of the common stock on the date prior to conversion with a floor price on such conversions of \$0.07 per share. Effective March 31, 2014, the holder converted this note and all related accrued interest into 302,043 shares of our common stock at a conversion price of \$0.16 per share.

Securities Issued for Services

We have issued securities in payment of services to reduce our obligations and to avoid using our cash resources. In the fiscal year ended March 31, 2014 we issued 3,071,150 common shares for services of which 1,568,124 were restricted and were for investor relations services and corporate communications services. Included in the 3,071,150 common shares issued for services are 1,503,026 shares, registered under Form S-8 registration statements, which were issued as follows: 71,140 for financial consulting, 419,069 for scientific consulting and 1,012,817 for legal services. The average price discount of common shares issued for these services, weighted by the number of shares issued for services in this period, was approximately 16.0%.

Securities Issued for Debt

We have also issued securities for debt to reduce our obligations to avoid using our cash resources. In the fiscal year ended March 31, 2014 we issued 10,574,024 restricted common shares for repayment in full of notes, including accrued interest, in the aggregate amount of \$726,776. The price discount of the common stock issued for debt was approximately 43.2%.

Prospects for Debt Conversion

We seek, where possible, to convert our debt and accounts payable to stock and/or warrants in order to reduce our cash liabilities. Our success at accomplishing this depends on several factors including market conditions, investor acceptance and other factors, including our business prospects. All conversions are done under an exemption from registration under Section 4(a)(2) of the Securities Act of 1933, as amended.

Going Concern

Our independent registered public accounting firm has stated in their audit report on our March 31, 2014 consolidated financial statements that our working capital deficiency and our accumulated deficit are conditions that, among others, raise substantial doubt about our ability to continue as a going concern.

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Three and Six-Month Periods Ended September 30, 2014 and 2013*Results of Operations*Three Months Ended September 30, 2014 Compared to the Three Months Ended September 30, 2013

Revenues

We recorded government contract revenue in the three months ended September 30, 2014 and 2013. This revenue arose from work performed under our government contract with the Defense Advanced Research Projects Agency and our subcontract with Battelle Memorial Institute as follows:

	Three Months Ended 9/30/14	Three Months Ended 9/30/13	Change in Dollars
Defense Advanced Research Projects Agency contract	\$444,723	\$613,143	\$(168,420)
Battelle Memorial Institute subcontract	34,352	31,744	2,608
Total government contract revenue	\$479,075	\$644,887	\$(165,812)

Defense Advanced Research Projects Agency Contract

We entered into a contract with the Defense Advanced Research Projects Agency on September 30, 2011. Under the Defense Advanced Research Projects Agency award, we have been engaged to develop a therapeutic device to reduce the incidence of sepsis, a fatal bloodstream infection that often results in the death of combat-injured soldiers. The award from the Defense Advanced Research Projects Agency was a fixed-price contract with potential total payments to us of \$6,794,389 over the course of five years. Fixed price contracts require the achievement of multiple, incremental milestones to receive the full award during each year of the contract. Under the terms of the contract, we will perform certain incremental work towards the achievement of specific milestones against which we will invoice the government for fixed payment amounts.

Originally, only the base year (year one contract) was effective for the parties, however, the Defense Advanced Research Projects Agency subsequently exercised the option on the second, third and fourth years of the contract. The Defense Advanced Research Projects Agency has the option to enter into the contract for year five. The milestones are comprised of planning, engineering and clinical targets, the achievement of which in some cases will require the

participation and contribution of third party participants under the contract. There can be no assurance that we alone, or with third party participants, will meet such milestones to the satisfaction of the government and in compliance with the terms of the contract or that we will be paid the full amount of the contract revenues during any year of the contract term. We commenced work under the contract in October 2011.

Due to budget restrictions within the Department of Defense, on February 10, 2014, the Defense Advanced Research Projects Agency reduced the scope of our contract in years three through five of the contract. The reduction in scope focused our research on exosomes, viruses and blood processing instrumentation. This scope reduction will reduce the possible payments under the contract by \$858,491 over years three through five.

During the three months ended September 30, 2014 we invoiced the Defense Advanced Research Projects Agency for three milestones totaling \$444,723 while in the three months ended September 30, 2013, we invoiced the Defense Advanced Research Projects Agency for three milestones totaling \$613,143.

Operating Expenses

Consolidated operating expenses for the three months ended September 30, 2014 were \$1,080,267 in comparison with \$874,683 for the comparable quarter a year ago. This increase of \$205,584 was due to increases in payroll and related expenses of \$139,505 and increases in general and administrative expenses of \$84,769, which were partially offset by a decrease in professional fees of \$18,690.

The \$139,505 increase in payroll and related expenses was primarily due to the Exosome Sciences, Inc. payroll of \$137,257. Other factors were an increase in stock-based compensation of \$14,980 and a decrease in cash-based compensation at Aethlon of \$12,732.

The \$84,769 increase in general and administrative expenses was due to general and administrative expenses at Exosome Sciences, Inc. of \$45,986. We also had an increase of \$56,617 in our non-Defense Advanced Research Projects Agency-related general and administrative expenses. Those increases were partially offset by a decrease in our Defense Advanced Research Projects Agency-related general and administrative expenses of \$17,834.

The \$18,690 decrease in our professional fees was due to a decrease in our Defense Advanced Research Projects Agency-related professional fees of \$48,188, which was partially offset by increases of \$20,675 in Exosome Sciences, Inc. professional fees and of \$8,823 of our non- Defense Advanced Research Projects Agency-related professional fees.

Other Expense

Other expense consists primarily of losses on extinguishment of debt, the change in the fair value of our derivative liability, other expense and interest expense. Other expense for the three months ended September 30, 2014 was other expense of \$287,001 in comparison with other expense of \$3,119,874 for the comparable quarter a year ago.

Loss on Extinguishment of Debt and Other

We recorded a loss on extinguishment of debt of \$65,493 for the three months ended September 30, 2014 that related to the conversion to equity of \$45,906 in principal and accrued interest related to a note payable. The three months ended September 30, 2013 contained \$17,467 in losses on debt conversion.

The three months ended September 30, 2014 also included a charge of \$143,363 for the change in fair value related to the extension of the warrants of a note holder in exchange for a postponement in the agreed payment date of his notes.

Change in Fair Value of Derivative Liability

We did not record a change in the fair value of derivative liabilities in the three months ended September 30, 2014. For the three months ended September 30, 2013, the change in the estimated fair value of derivative liability was a loss of \$2,992,002.

Interest Expense

Interest expense was \$78,145 for the three months ended September 30, 2014 compared to \$110,405 in the corresponding prior period, a decrease of \$32,260. The various components of our interest expense are shown in the following table:

	Quarter Ended 9/30/14	Quarter Ended 9/30/13	Change
Interest expense	\$66,585	\$108,723	\$(42,138)
Amortization of deferred financing costs	11,560	–	11,560
Amortization of note discounts	–	1,682	(1,682)
Total interest expense	\$78,145	\$110,405	\$(32,260)

As noted in the above table, the most significant factor in the \$32,260 decrease in interest expense was the \$42,138 decrease in the interest expense that was primarily due to lower levels of notes outstanding in the 2014 period. Other smaller factors in the change in our total interest were an increase in the amortization of deferred financing costs of \$11,560 and a \$1,682 reduction in the amortization of note discounts.

Net Loss

As a result of the increased expenses noted above, our net loss before noncontrolling interests was approximately \$888,000 for the quarter ended September 30, 2014 compared to the net loss before noncontrolling interests of approximately \$3,350,000 in the quarter ended September 30, 2013.

Basic and diluted loss attributable to common stockholders were (\$0.00) for the three month period ended September 30, 2014 compared to (\$0.02) for the three month period ended September 30, 2013.

Six Months Ended September 30, 2014 Compared to the Six Months Ended September 30, 2013

Revenues

We recorded government contract revenue in the six months ended September 30, 2014 and 2013. This revenue arose from work performed under our government contract with the Defense Advanced Research Projects Agency and our subcontract with Battelle Memorial Institute as follows:

	Six Months Ended 9/30/14	Six Months Ended 9/30/13	Change in Dollars
Defense Advanced Research Projects Agency contract	\$444,723	\$808,739	\$(364,016)
Battelle Memorial Institute subcontract	85,648	31,744	53,904
Total government contract revenue	\$530,371	\$840,483	\$(310,112)

Defense Advanced Research Projects Agency Contract

We entered into a contract with the Defense Advanced Research Projects Agency on September 30, 2011. Under the Defense Advanced Research Projects Agency award, we have been engaged to develop a therapeutic device to reduce the incidence of sepsis, a fatal bloodstream infection that often results in the death of combat-injured soldiers. The award from the Defense Advanced Research Projects Agency was a fixed-price contract with potential total payments to us of \$6,794,389 over the course of five years. Fixed price contracts require the achievement of multiple, incremental milestones to receive the full award during each year of the contract. Under the terms of the contract, we will perform certain incremental work towards the achievement of specific milestones against which we will invoice the government for fixed payment amounts.

Originally, only the base year (year one contract) was effective for the parties; however, the Defense Advanced Research Projects Agency subsequently exercised the option on the second, third and fourth years of the contract. The Defense Advanced Research Projects Agency has the option to enter into the contract for year five. The milestones are comprised of planning, engineering and clinical targets, the achievement of which in some cases will require the participation and contribution of third party participants under the contract. There can be no assurance that we alone, or with third party participants, will meet such milestones to the satisfaction of the government and in compliance with the terms of the contract or that we will be paid the full amount of the contract revenues during any year of the contract term. We commenced work under the contract in October 2011.

Due to budget restrictions within the Department of Defense, on February 10, 2014, the Defense Advanced Research Projects Agency reduced the scope of our contract in years three through five of the contract. The reduction in scope focused our research on exosomes, viruses and blood processing instrumentation. This scope reduction will reduce the possible payments under the contract by \$858,491 over years three through five.

During the six months ended September 30, 2014 we invoiced the Defense Advanced Research Projects Agency for three milestones totaling \$444,723 while in the six months ended September 30, 2013, we invoiced the Defense Advanced Research Projects Agency for four milestones totaling \$808,739.

Operating Expenses

Consolidated operating expenses for the six months ended September 30, 2014 were \$2,303,571 in comparison with \$1,854,075 for the comparable period a year ago. This increase of \$449,496 was due to increases in payroll and related expenses of \$301,560, increases in professional fees of \$58,853 and increases in general and administrative expenses of \$89,083.

The \$301,560 increase in payroll and related expenses was primarily due to the Exosome Sciences, Inc. payroll of \$260,968. Other factors were an increase in stock-based compensation of \$70,079 due to vesting of stock option grants while cash-based compensation at Aethlon decreased by \$29,487 from the 2013 period.

The \$58,853 increase in our professional fees was partially due to Exosome Sciences, Inc. professional fees of \$87,719 and an increase of \$69,269 for non-Defense Advanced Research Projects Agency-related professional fees at Aethlon. Those increases at Aethlon were primarily due to a \$71,432 increase in legal fees, largely due to increased patent-related activity. Those increases were offset by a decrease in Defense Advanced Research Projects Agency-related professional fees of \$98,135.

The \$89,083 increase in general and administrative expenses was primarily due to general and administrative expenses at Exosome Sciences, Inc. of \$96,987.

Other Expense

Other expense consists primarily of losses on extinguishment of debt, the change in the fair value of our derivative liability, other expense and interest expense. Other (income) expense for the six months ended September 30, 2014 was other expense of \$2,819,285 in comparison with other expense of \$2,639,576 for the comparable period a year ago.

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Loss on Extinguishment of Debt and Other

We recorded a loss on extinguishment of debt of \$2,531,123 for the six months ended September 30, 2014. That loss arose from the payments of accrued interest on our 12% Series A convertible notes that were in the form of units (common stock plus warrants) combined with a loss that related to the conversion to equity of \$45,906 in principal and accrued interest related to a note payable. The three months ended September 30, 2013 contained \$40,256 in losses on debt conversion.

The three months ended September 30, 2014 also included a charge of \$143,363 for the change in fair value related to the extension of the warrants of a note holder in exchange for a postponement in the agreed payment date of his notes.

Change in Fair Value of Derivative Liability

We did not record a change in the fair value of derivative liabilities in the six months ended September 30, 2014 and all derivative liabilities were extinguished as of June 30, 2014. For the six months ended September 30, 2013, the change in the estimated fair value of derivative liability was a loss of \$2,382,877.

Interest Expense

Interest expense was \$144,799 for the six months ended September 30, 2014 compared to \$216,443 in the corresponding prior period, a decrease of \$71,644. The various components of our interest expense are shown in the following table:

	Six Months Ended 9/30/14	Six Months Ended 9/30/13	Change
Interest expense	\$ 123,297	\$ 211,865	\$(88,568)
Amortization of deferred financing costs	21,502	863	20,639
Amortization of note discounts	—	3,715	(3,715)
Total interest expense	\$ 144,799	\$ 216,443	\$(71,644)

As noted in the above table, the most significant factor in the \$71,644 decrease in interest expense was the \$88,568 decrease in the interest expense that was primarily due to lower levels of notes outstanding in the 2014 period. Other smaller factors in the change in our total interest were an increase in the amortization of deferred financing costs of

\$20,639, which was partially offset by a reduction in the amortization of note discounts.

Net Loss

As a result of the increased expenses noted above, our net loss before noncontrolling interests for the six months ended September 30, 2014 was approximately \$4,592,000 compared to approximately \$3,653,000 for the six month period ended September 30 2013.

Basic and diluted loss attributable to common stockholders were (\$0.02) for the six month period ended September 30, 2014 compared to (\$0.02) for the period ended September 30, 2013.

Liquidity and Capital Resources

At September 30, 2014, we had a cash balance of \$526,187 and a working capital deficit of \$2,495,767. This compares to a cash balance of \$1,250,279 and a working capital deficit of \$14,169,471 at March 31, 2014. Between October 1, 2014 and December 31, 2014, we raised aggregate proceeds of \$4,083,579 through equity issuances and raised \$415,000 through the issuance of convertible notes. Over that same period, we collected \$247,361 under our Defense Advanced Research Projects Agency contract and under the Battelle Memorial Institute subcontract we billed \$33,434 and collected \$29,519. At December 31, 2014, we had a cash balance of approximately \$2,800,000, which we believe may be sufficient to fund the initial phase of our recently approved human clinical trial in the U.S. but will not be sufficient to fund future phases of our human trial or potential additional human trials nor to meet our funding requirements during the next twelve months. We must obtain significant additional financing to provide a sufficient source of operating capital in future periods and to allow us to continue to operate as a going concern.

Cash Flows

Cash flows from operating, investing and financing activities, as reflected in the accompanying Condensed Consolidated Statements of Cash Flows, are summarized as follows (in thousands):

	(In thousands)	
	For the six months	
	ended	
	September	September
	30,	30,
	2014	2013
Cash (used in) provided by:		
Operating activities	\$(1,394)	\$ (745)
Investing activities	-	-
Financing activities	670	628
Net (decrease) in cash	\$(724)	\$ (117)

Net Cash from Operating Activities.

We used cash in our operating activities due to our losses from operations. Net cash used in operating activities was approximately \$1,394,000 in the six months ended September 30, 2014 compared to \$745,000 in the six months ended September 30, 2013, an increase of \$649,000. The \$649,000 increase was primarily due to our increased operating loss.

Net Cash from Investing Activities.

We did not have any investing activities during either period.

Net Cash from Financing Activities.

Net cash generated from financing activities increased from approximately \$628,000 in the six months ended September 30, 2013 to \$670,000 in the six months ended September 30, 2014. The only financing activity in the 2014 periods was the issuance of common stock, while in the 2013 period, financing activities included \$400,000 in proceeds from the issuance of notes payable.

An increase in working capital during the six months ended September 30, 2014 in the amount of approximately \$11,684,000 changed our negative working capital position to approximately (\$2,496,000) at September 30, 2014 from a negative working capital of approximately (\$14,169,000) at March 31, 2014. The most significant factors in the increase in working capital noted above were a decrease in derivative liability of approximately \$10,679,000 and a reduction in the current portion of our convertible notes payable and notes payable of approximately \$1,096,000.

At the date of this filing, we plan to invest significantly into purchases of our raw materials and into our contract manufacturing arrangement subject to successfully raising additional capital.

Critical Accounting Policies

Use of Estimates

The preparation of consolidated financial statements in conformity with GAAP 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 the most difficult, subjective or complex judgments, form the basis for the accounting policies deemed to be most critical to us. These critical accounting estimates relate to revenue recognition, stock purchase warrants issued with notes payable, beneficial conversion feature of convertible notes payable, impairment of intangible assets and long lived assets, stock compensation, deferred tax asset valuation allowance, and contingencies.

Fair Value Measurements

We measure the fair value of applicable financial and non-financial instruments based on the following fair value hierarchy:

- Level 1: Quoted market prices in active markets for identical assets or liabilities.
- Level 2: Observable market based inputs or unobservable inputs that are corroborated by market data.
- Level 3: Unobservable inputs that are not corroborated by market data.

The hierarchy noted above requires us to minimize the use of unobservable inputs and to use observable market data, if available, when determining fair value.

The fair value of derivative liabilities is determined based on unobservable inputs that are not corroborated by market data, which is a Level 3 classification. We record derivative liabilities on our balance sheet at fair value with changes in fair value recorded in our consolidated statements of operations.

Revenue Recognition

With respect to revenue recognition, we entered into a government contract with the Defense Advanced Research Projects Agency and have recognized revenue during the fiscal years ended March 31, 2014 and 2013 of \$1,466,482 and \$1,230,004, respectively, under such contract. We adopted the Milestone method of revenue recognition for the Defense Advanced Research Projects Agency contract under ASC 605-28 “Revenue Recognition – Milestone Method” and we believe we meet the requirements under ASC 605-28 for reporting contract revenue under the Milestone Method for the fiscal years ended March 31, 2014 and 2013.

We also recognize revenue under for a secondary smaller contract under a time and materials non-fixed price basis where we recognize revenue as the services are performed.

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Stock Purchase Warrants

We grant warrants in connection with the issuance of certain notes payable and other financing transactions. When such warrants are classified as equity, we measure the relative estimated fair value of such warrants which represents a discount from the face amount of the notes payable. Such discounts are amortized to interest expense over the term of the notes. We analyze such warrants for classification as either equity or derivative liabilities, and value them based on binomial lattice models.

Beneficial Conversion Feature of Notes Payable

The convertible feature of certain notes payable provides for a rate of conversion that is below market value. Such feature is normally characterized as a "beneficial conversion feature of which we measure the estimated fair value in circumstances in which the conversion feature is not required to be separated from the host instrument and accounted for separately, and record that value in the consolidated financial statements as a discount from the face amount of the notes. Such discounts are amortized to interest expense over the term of the notes.

Share-based Compensation

We account for share-based compensation awards using the fair-value method and record such expense based on the grant date fair value in the consolidated financial statements over the requisite service period.

Derivative Instruments

We evaluate free-standing derivative instruments (or embedded derivatives) to properly classify such instruments within equity or as liabilities in our financial statements. Our policy is to settle instruments indexed to our common shares on a first-in-first-out basis.

The classification of a derivative instrument is reassessed at each reporting date. If the classification changes as a result of events during a reporting period, the instrument is reclassified as of the date of the event that caused the reclassification. There is no limit on the number of times a contract may be reclassified.

Instruments classified as derivative liabilities are remeasured each reporting period (or upon reclassification) and the change in fair value is recorded on our consolidated statement of operations in other expense (income).

Deferred Tax Asset Valuation Allowance

Deferred tax assets are recognized for the future tax consequences attributable to the difference between the consolidated financial statements and their respective tax basis. Deferred income taxes reflect the net tax effects of (a) temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts reported for income tax purposes, and (b) tax credit carryforwards. We record a valuation allowance for deferred tax assets when, based on our best estimate of taxable income (if any) in the foreseeable future, it is more likely than not that some portion of the deferred tax assets may not be realized.

Off-Balance Sheet Arrangements

We have not entered into any off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that is material to investors.

Material Changes During the Period September 30, 2014 to December 31, 2014

In addition to the billings and collections on our government contracts noted above, the following discussion details specific transactions we entered into after September 30, 2014 that effect our liquidity and capital resources:

Debt Reduction

Subsequent to September 30, 2014, we paid off the remaining principal and interest balances on the two remaining July and August 2011 10% Convertible Notes, which had been classified as being in default, with cash payments totaling \$382,748.

Subsequent to September 30, 2014, we paid off in full the outstanding principal balance and interest balance on Law Firm Note 1 with a cash payment of \$50,000 and an issuance of 170,020 common shares.

Subsequent to September 30, 2014, we paid an aggregate of \$503,313 in principal and accrued interest on eight other outstanding notes. As a result, seven of the eight notes were paid in full. We owe an additional \$37,813 under the eighth note, which we expect to pay in full in January 2015.

Note Conversions

Subsequent to September 30, 2014, we issued an aggregate of 14,237,261 shares of common stock to two accredited investors upon the conversion of an aggregate of \$597,965 of unpaid principal and accrued interest due under promissory notes we previously issued to the investors. The conversion price per share was \$0.042

Subsequent to September 30, 2014, we issued an aggregate of 5,625,000 shares of common stock to convert in full the outstanding principal balance of \$225,000 and interest balance of \$11,250 on the remaining note from 2010 through the issuance of 5,625,000 shares of common stock. The conversion price per share was \$0.042.

Issuance of Convertible Notes

Subsequent to September 30, 2014, we sold to two accredited investors (i) convertible promissory notes in the aggregate principal amount of \$527,780 and (ii) five year warrants to purchase up to 2,356,160 shares of common stock at a fixed exercise price of \$0.168 per share. The convertible promissory notes bear interest at the annual rate of 10% and mature on April 1, 2016. The aggregate gross cash proceeds to us were \$415,000 after subtracting legal fees of \$35,000; the balance of the principal amount of the notes represents a \$27,780 due diligence fee and an original issuance discount. The convertible promissory notes are convertible at the option of the holders into shares of our common stock at a fixed price of \$0.112 per share, for up to an aggregate of 4,712,321 shares of common stock.

The following table provides a comparison of our convertible notes payable at December 31, 2014 and at September 30, 2014:

	Convertible Notes Payable as of December 31, 2014		Convertible Notes Payable as of September 30, 2014	
	Principal	Accrued Interest	Principal	Accrued Interest
Convertible Notes Payable - Current Portion:				
October & November 2009 10% Convertible Notes	\$—	\$—	\$50,000	\$28,598
April 2010 10% Convertible Note	—	—	75,000	35,188
July and August 2011 10% Convertible Notes, past due	—	—	283,421	96,728
Law Firm Note	—	—	75,000	9,479
Total - Convertible Notes Payable - Current Portion	—	—	483,422	169,993
Convertible Notes Payable - Non-Current Portion:				
November 2014 10% Convertible Notes	527,780	8,063	—	—
Amended and Restated Series A 12% Convertible notes	—	—	225,000	9,000
September 2010 12% Convertible Notes	—	—	317,072	9,513
April 2011 12% Convertible Notes	202,159	2,680	448,448	13,454
Total - Convertible Notes Payable - Non-Current Portion	729,939	10,743	990,520	31,967
Total Convertible Notes Payable	\$729,939	\$10,743	\$1,473,941	\$201,860

Common Stock Issuances

Subsequent to September 30, 2014, we issued 374,295 shares of common stock pursuant to our S-8 registration statement covering our Amended 2010 Stock Plan at an average price of \$0.146 per share in payment for legal and scientific consulting services valued at \$54,800 based on the value of the services provided.

Equity Unit Investments

Subsequent to September 30, 2014, we issued and sold to eight accredited investors units consisting of (a) 100,000 restricted shares of our common stock at prices per share ranging from \$0.105 to \$0.114 and (b) a five-year warrant to purchase 50,000 shares of common stock at exercise prices ranging from \$0.154 to \$0.167 per share. In total, the investors purchased for cash an aggregate of \$501,700 of units. The investors acquired an aggregate of 4,506,250 shares of common stock and warrants to acquire up to an aggregate of 2,253,125 shares of common stock.

Explanation of Responses:

Subsequent to September 30, 2014, we issued to an accredited investor units consisting of an aggregate of 1,835,798 shares of common stock and warrants to acquire up to an aggregate of 1,837,798 shares of common stock at an exercise price of \$0.103 per share. The units were issued to the investor upon the conversion of an aggregate of \$189,087 of unpaid principal and accrued interest due under two promissory notes we previously issued to the investor. The amounts converted represented the entire principal and interest outstanding under the notes and the notes held by that holder were retired.

Subsequent to September 30, 2014, we sold \$3,300,000 of units, comprised of common stock and warrants, to three affiliated institutional investors at a price of \$0.30 per unit. Each unit consists of one share of common stock and a warrant to purchase 1.2 shares of common stock at an exercise price per share of \$0.30. We sold a total of 11,000,000 shares of common stock and warrants to purchase 13,200,000 shares of common stock in the financing.

Roth Capital Partners, LLC served as sole placement agent for our recent financing and received a cash fee of \$231,000, expense reimbursement of \$25,000, and a five-year warrant to purchase 550,000 shares of common stock at an exercise price of \$0.30 per share for its services in the financing. In addition, we paid \$10,000 in legal expenses to the investors' counsel. We also paid \$32,572 to our counsel related to this financing. The net proceeds to us after the placement fee and legal fees were \$3,001,429.

Warrant Exercises and Issuance of New Warrants upon Exercise

Subsequent to September 30, 2014, we issued an aggregate of 5,671,119 shares of common stock and seven-year warrants to issue up to an aggregate of 5,671,119 shares of common stock at exercise prices ranging from \$0.093 to \$0.116 per share to eight accredited investors. One of the investors is Dr. Chetan Shah, one of our directors. We issued the common stock and warrants to the investors upon the cash exercise of previously issued warrants held by them. The investors paid an aggregate of \$579,251 upon exercise of the previously outstanding warrants at exercise prices ranging from \$0.093 to \$0.115 per share.

Warrant Exercises

Subsequent to September 30, 2014, we issued an aggregate of 21,516,640 shares of common stock to accredited investors upon the exercise of previously issued warrants. The warrants were exercised on a cashless or "net" basis. Accordingly, we did not receive any proceeds from such exercises. The cashless exercise of such warrants resulted in the cancellation of previously issued warrants to purchase an aggregate of 30,265,208 shares of common stock.

Stock Option Exercises

Subsequent to September 30, 2014, two former employees exercised stock options to purchase 50,000 common shares through a cash payment of \$9,500 with an exercise price of \$0.19 per share.

We do not expect revenue from operations will be sufficient to satisfy our funding requirements in the near term, and accordingly, our ability to continue operations and 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. Future capital requirements will depend upon many factors, including progress with pre-clinical testing and clinical trials, the number and breadth of our clinical 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, as well as 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.

Should the U.S. Government elect not to exercise the option for year five of our Defense Advanced Research Projects Agency contract, the effect may be material to us. The loss of revenues from the Defense Advanced Research Projects Agency contract would have a material impact on our revenues, operating cash flows and liquidity.

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DIRECTORS AND EXECUTIVE OFFICERS

The names, ages and positions of our directors and executive officers as of December 31, 2014 are listed below:

NAMES	TITLE OR POSITION	AGE
James A. Joyce (1)	Chairman, Chief Executive Officer and Secretary	53
Richard H. Tullis, PhD (2)	Vice President, Chief Science Officer and Director	69
Rodney S. Kenley (3)	President and Director	64
James B. Frakes (4)	Chief Financial Officer and Senior Vice President - Finance	57
Franklyn S. Barry, Jr.	Director	75
Edward G. Broenniman	Director	78
Chetan S. Shah, MD	Director	46

(1) Effective June 1, 2001, Mr. Joyce was appointed our President and Chief Executive Officer, replacing Mr. Barry, who continues as a member of the Board of Directors. Mr. Joyce resigned from the position of President upon the appointment of Mr. Kenley to such position on October 27, 2010.

(2) Effective June 1, 2001, Dr. Tullis was appointed as our Chief Science Officer.

(3) Effective October 27, 2010, Mr. Kenley was appointed as our President.

(4) Effective September 27, 2010, Mr. Frakes was appointed as our Chief Financial Officer.

Certain additional information concerning the individuals named above is set forth below. This information is based on information furnished us by each individual noted.

Resumes of Management

James A. Joyce, Chairman, CEO and Secretary.

Mr. Joyce is the founder of Aethlon Medical, Inc. and has been the Chairman of the Board and Secretary since March 1999. On June 1, 2001, our Board of Directors appointed Mr. Joyce with the additional role of CEO. Mr. Joyce also serves as the Executive Chairman of Exosome Sciences, Inc. In 1992, Mr. Joyce founded and was the sole stockholder of James Joyce & Associates, an organization that provided management consulting and corporate finance advisory services to CEOs and CFOs of publicly traded companies. Previously, from 1989 to 1991, Mr. Joyce was Chairman and Chief Executive Officer of Mission Labs, Inc. Prior to that Mr. Joyce was a principal in charge of U.S. operations for London Zurich Securities, Inc. Mr. Joyce is a graduate of the University of Maryland.

Richard H. Tullis, Ph.D., Vice President, Chief Science Officer

Dr. Tullis has been Vice President and a director of our company since January 2000 and Chief Science Officer since June 2001. Dr. Tullis has extensive biotechnology management and research experience, and is the founder of Syngen Research, formerly a wholly owned subsidiary of Aethlon Medical, Inc. Previously, Dr. Tullis co-founded Molecular Biosystems, Inc., a former NYSE company. At Molecular Biosystems, Dr. Tullis was Director of Oligonucleotide Hybridization, Senior Research Scientist and Member of the Board of Directors. In research, Dr. Tullis developed and patented the first application of oligonucleotides to antisense antibiotics and developed new methods for the chemical synthesis of DNA via methoxy-phosphorochloridites. Dr. Tullis also co-developed the first applications of covalently coupled DNA-enzyme conjugates using synthetic oligonucleotides during his tenure at Molecular Biosystems. In 1985, Dr. Tullis founded, and served as President and CEO of Synthetic Genetics, Inc., a pioneer in custom DNA synthesis, which was sold to Molecular Biology Resources in 1991. Dr. Tullis also served as interim-CEO of Genetic Vectors, Inc., which completed its IPO under his management, and was co-founder of DNA Sciences, Inc., a company that was eventually acquired by Genetic Vectors. Dr. Tullis received his Ph.D. in Biochemistry and Cell Biology from the University of California at San Diego, and has done extensive post-doctoral work at UCSD, USC, and the University of Hawaii.

Rodney S. Kenley, President and Director

Mr. Kenley has been President and a Director since October 2010. He has 34 years of experience in healthcare, most of which have been spent in the extracorporeal blood purification arena. Mr. Kenley held several positions at Baxter Healthcare (Travenol) from 1977 through 1990 including International Marketing Manager, Business Unit Manager for Peritoneal and Hemodialysis products, Manager of New Business Development, Director of Worldwide Product Planning, Director of Advanced Product Development, and VP of Electronic Drug Infusion. During this tenure he conceived of and managed the launch of several new products that have been highly commercially successful including the HomeChoice peritoneal dialysis cyclor.

Mr. Kenley founded Aksys Ltd. in January 1991 to develop and commercialize his concept of a daily home hemodialysis system which was commercially launched in 2002 as the PHD system. In 2004, Mr. Kenley initiated the development of a second-generation home hemodialysis system in partnership with DEKA Research & Development Corporation in Manchester, New Hampshire. In 2007, the assets of Aksys Ltd. were acquired by DEKA, where Mr. Kenley was employed prior to joining Aethlon Medical, Inc.

Mr. Kenley is the recipient of over 30 patents.

Mr. Kenley received his Bachelor of Arts degree in Biology and Chemistry from Wabash College, a Masters of Science degree in Molecular Biology from Northwestern University and a Masters of Management from the Kellogg School of Management, also at Northwestern University.

James B. Frakes, Chief Financial Officer and Senior Vice President – Finance

Mr. Frakes joined Aethlon Medical, Inc. in January 2008 and brought 16 consecutive years of financial responsibility for publicly traded companies, as well as specific knowledge and experience in equity and debt transactions, acquisitions, public reporting and Sarbanes-Oxley Section 404 internal control requirements. Mr. Frakes also serves as the Chief Financial Officer of Exosome Sciences, Inc.

He previously served as the CFO for Left Behind Games Inc., a start-up video game company. Prior to 2006, he served as CFO of NTN Buzztime, Inc., an interactive entertainment company with \$40 million in sales, where he played a key role in acquisitions that doubled the company's revenue. Mr. Frakes received an MBA from the University of Southern California and completed his BA with Honors at Stanford University.

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Franklyn S. Barry, Jr.

Mr. Barry has over 30 years of experience in managing and building companies. He was President and Chief Executive Officer of Hemex from April 1997 through May 31, 2001 and our President and CEO from March 10, 1999 to May 31, 2001, when he returned to consulting until he retired in 2013. He became a director of Aethlon Medical, Inc. on March 10, 1999. From 1994 to April 1997, Mr. Barry was a private consultant. Included among his prior experiences are tenures as President of Fisher-Price and as co-founder and CEO of Software Distribution Services, which today operates as Ingram Micro-D, an international distributor of personal computer products. Mr. Barry serves on the Board of Directors of Merchants Mutual Insurance Company.

Edward G. Broenniman

Mr. Broenniman became a director of Aethlon Medical, Inc. in March 1999. Mr. Broenniman has 30 years of management and executive experience with high-tech, privately held growth companies where he has served as a CEO, COO, or corporate advisor, using his expertise to focus management on increasing profitability and stockholder value. He has been the Managing Director of The Piedmont Group, LLC, a venture advisory firm, since 1978. Mr. Broenniman recently served on the Board of Directors of publicly traded QuesTech (acquired by CACI International), and currently serves on the Boards of two privately held firms. His nonprofit Boards are the Dingman Center for Entrepreneurship's Board of Advisors at the University of Maryland, the National Association of Corporate Directors, National Capital Chapter and the Board of the Association for Corporate Growth, National Capital Chapter.

Chetan S. Shah, MD

Dr. Shah became a director of Aethlon Medical, Inc. in June 2013. Dr. Shah is a board certified Otolaryngologist. He is an Advisory Board Member at The Bank of Princeton, and a partner and Board member of the Surgery Center at Hamilton as well as Physician Management Systems and Princeton Eye & Ear, which he founded in 2009. Dr. Shah serves on the board of two other private companies. He holds teaching positions and serves on multiple hospital committees in the area and is on the Audiology and Speech Language Pathology Committee for the State of New Jersey. He also is a member of the Board of Medical Examiners for the State of New Jersey. Dr. Shah received his Bachelor's degree and Medical Degree from Rutgers University and Robert Wood Johnson Medical School.

Board of Directors

Our Board of Directors has the responsibility for establishing broad corporate policies and for overseeing our overall performance. Members of the Board are kept informed of our business activities through discussions with the CEO, President and other officers, by reviewing analyses and reports sent to them, and by participating in Board and

committee meetings. Our bylaws provide that each of the directors serves for a term that extends to our next annual meeting of stockholders. Our Board of Directors presently has an Audit Committee and a Compensation Committee, on each of which Messrs. Barry and Broenniman and Dr. Shah serve. Mr. Barry is Chairman of the Audit Committee, and Dr. Shah is Chairman of the Compensation Committee.

In July 2012, our Board of Directors approved a board compensation program that modifies and supersedes the 2005 Directors Compensation Program, which was previously in effect. Under the 2012 program, in which only non-employee directors may participate, an eligible director will receive a grant of \$35,000 worth of ten year options to acquire shares of common stock, with such grant being valued at the exercise price based on the average of the closing bid prices of the common stock for the five trading days preceding the first day of the fiscal year. In addition, under this new program, eligible directors will receive cash compensation equal to \$500 for each committee meeting attended and \$1,000 for each formal board meeting attended.

In the fiscal year ended March 31, 2013, our Board of Directors granted ten-year options to acquire an aggregate of 1,667,105 shares of our common stock, all with an exercise price of \$0.076 per share, to our four outside directors under the new 2012 program.

In the fiscal year ended March 31, 2014, our Board of Directors granted ten-year options to acquire an aggregate of 1,595,536 shares of our common stock, all with an exercise price of \$0.082 per share, to our five outside directors under the new 2012 program.

At March 31, 2014 we had issued 1,337,825 options under the old 2005 program to outside directors and 3,965,450 options to employee-directors, 514,550 outside directors' options had been forfeited, 250,000 outside directors' options had been exercised and 3,671,550 options remained outstanding.

On June 6, 2014, our Board of Directors approved certain changes to the 2012 program. Under this new program, a new eligible director will receive an initial grant of \$50,000 worth of options to acquire shares of common stock, with such grant being valued at the exercise price based on the average of the closing bid prices of the common stock for the five trading days preceding the first day of the fiscal year. These options will have a term of ten years and will vest 1/3 upon grant and 1/3 upon each of the first two anniversaries of the date of grant. In addition, at the beginning of each fiscal year, each existing director eligible to participate in the modified new 2012 program also will receive a grant of \$35,000 worth of options valued at the exercise price based on the average of the closing bid prices of the common stock for the five trading days preceding the first day of the fiscal year. Such options will vest on the first anniversary of the date of grant. In lieu of per meeting fees, eligible directors will receive an annual board retainer fee of \$30,000. The modified new 2012 program also provides for the following annual retainer fees: Audit Committee Chair - \$5,000, Compensation Committee chair - \$5,000, Audit Committee member - \$4,000, Compensation Committee member - \$4,000 and lead independent director - \$15,000.

Family Relationships

There are no family relationships between or among the directors, executive officers or persons nominated or chosen by us to become directors or executive officers.

There are no arrangements or understandings between any two or more of our directors or executive officers or between any of our directors or executive officers and any other person pursuant to which any director or officer was or is to be selected as a director or officer, and there is no arrangement, plan or understanding as to whether non-management stockholders will exercise their voting rights to continue to elect the current Board of Directors. There are also no arrangements, agreements or understandings between non-management stockholders that may directly or indirectly participate in or influence the management of our affairs.

Science Advisory Board

Our Science Advisory Board is organized in three groups: the Extracorporeal Therapy Advisory Board, the Sepsis and Inflammation Advisory Board and the Cancer Advisory Board. The role of the Science Advisory Board is to provide scientific guidance related to the development of our Aethlon ADAPT technology. Unlike the members of our Board of Directors, the Science Advisory Board members are not involved in the management or operations of our company. Members of the Science Advisory Board are paid stipends for attending meetings.

Extracorporeal Therapy Advisory Board Sepsis and Inflammation Advisory Board Cancer Advisory Board

Gregory T. A. Kovacs, M.D., Ph.D.

Irshad H. Chaudry, Ph.D.

Laszlo Radvanyi, Ph.D.

John A. Kellum, M.D.

Larry D. Cowgill, D.V.M., Ph.D.

Nathan W. Levin, M.D.

Charles J. Fisher, Jr., M.D.

Claudio Ronco, M.D.

Geert Schmid-Schnein, Ph.D.

David M. Ward, M.D.

Extracorporeal Therapy Advisory Board

Gregory T.A. Kovacs, M.D., Ph.D.

Dr. Kovacs is a Professor of Electrical Engineering at Stanford University with a courtesy appointment in the Department of Medicine. He received a BSc degree in Electrical Engineering from the University of British Columbia, an MS degree in Bioengineering from the University of California, Berkeley, and a PhD and an MD degree from Stanford University. Dr. Kovacs is the Director of Medical Device Technologies for the Astrobiology Program at the NASA Ames Research Center, and Principal Investigator for the NASA/Stanford National Center for Space Biological Technologies. This Center is charged with developing advanced medical devices to enable extended human spaceflight and instrumentation/payloads for biological experiments. Dr. Kovacs also has extensive industry experience including co-founding and providing technical guidance for several companies, including Cepheid in Sunnyvale, CA, supplier of advanced instrumentation for clinical and research nucleic acid diagnostics. Through Northrup Grumman, Cepheid supplies the automated biothreat detection systems in use by the United States Postal Service. He is a long-standing member of the Defense Sciences Research Council (Defense Advanced Research Projects Agency), and has served as Associate Chair and Chairman. In this capacity, he has led or co-led studies on a variety of topics from chemical and biological agent detection and decontamination, miniaturized biological instrumentation, jungle warfare technologies, and many others. Between 2008 and 2011, Dr. Kovacs was on leave from Stanford University to serve as director of the Microsystems Technology Office at the Defense Advanced Research Projects Agency.

John A. Kellum, M.D.

Dr. Kellum is a tenured professor of Critical Care Medicine at the University of Pittsburgh. He is a clinician scientist whose research interests span various aspects of Critical Care Medicine, but center in critical care nephrology (including acid-base, and renal replacement therapy), sepsis and multi-organ failure (including blood purification), and clinical epidemiology. His research has received continuous funding from the National Institutes of Health since 2001 and he has active funding from multiple different NIH Institutes. Dr. Kellum has authored more than 300 publications and has also edited several major textbooks including Critical Care Nephrology 2nd Edition (WB Saunders), and Stewart's Textbook of Acid-Base, 2nd Edition (www.acidbase.org). He has won several teaching awards, lectures widely, and has given more than 300 seminars and invited lectures related to his research. Dr. Kellum has been involved in the development of several clinical practice guidelines. He is a founding member and

past president of the Acute Dialysis Quality Initiative (www.ADQI.net) and is co-chair of the Kidney Diseases Improving Global Outcomes (KDIGO) clinical practice guideline on acute kidney injury (www.kdigo.org). Finally Dr. Kellum is a leader in electronic research especially in critical illness and is the Director of CARE (Center for Assistance in Research using the eRecord) also at the University of Pittsburgh.

Nathan W. Levin, M.D.

Dr. Levin is the Chairman, Research Board of the Renal Research Institute and Professor of Clinical Medicine, Albert Einstein College of Medicine. Past Medical and Research Director, Renal Research Institute (1997-2010). Dr. Levin is the Chair of the Selection Committee for the Lillian Jean Kaplan International Prize for Advancement in the Understanding of Polycystic Kidney Disease (PKD). He is the Co-Founder of Sustainable Kidney Care Foundation. Dr. Levin is an advisor to the Board of KidneyTel. He has lectured nationally and internationally on topics relating to chronic kidney disease (CKD) and hemodialysis. He is the Principal Investigator of the NIH sponsored study of Frequent Dialysis. Dr. Levin is currently an adjunct Professor of Medicine at the School of Medicine, The University of North Carolina at Chapel Hill. He is the Honorary Chair, Peking University, in Beijing, China. Dr. Levin contributes to the global CKD community in a variety of functions.

Claudio Ronco, M.D.

Dr. Ronco is Director of the Department of Nephrology at St. Bortolo Hospital in Vicenza. He is a member of the council of several scientific societies and is Editor in Chief of the International Journal of Artificial Organs. He has received numerous awards and honors, including the International Medal of Excellence from the National Kidney Foundation (NKF) and honorary membership of the Spanish Society of Nephrology (SSN). Dr. Ronco has organized several congresses and meetings in the area of nephrology and intensive care and is a member of several advisory groups for clinical trials and dialysis research. He has co-authored over 650 papers, 36 book chapters, 45 books and seven monographic journal issues, and has delivered more than 450 lectures at international meetings and universities. In 1989, Dr. Ronco was awarded his diploma in pediatric nephrology at the University of Naples, having achieved a specialized diploma in medical nephrology at the Post-graduate School of Internal Medicine at the University of Padua in 1979. He graduated in medicine from the University of Padua, having been an intern at the Institute of Clinical Internal Medicine at the same institution.

David M. Ward, M.D.

Dr. Ward trained in nephrology in Scotland and did a second fellowship in renal immunopathology at Scripps Research Foundation. Since 1977 he has been a member of the Division of Nephrology at UCSD. He directed the dialysis unit and clinical nephrology program at UCSD for 19 years, and has directed the therapeutic apheresis program for the last 22 years. At different times he has served the UCSD Medical School as Assistant Dean for Clinical Affairs, Chief of Staff of the Hospital, and Chairman of the UCSD Medical Group. Special interests include immunological diseases, glomerular diseases, transplantation medicine, apheresis medicine, hemodialysis technology, innovative extracorporeal blood circuits, and general clinical nephrology. He practices, publishes and teaches in these areas, including authoring chapters in standard textbooks such as "Rheumatology" and "Clinical Dialysis".

Sepsis and Inflammation Advisory Board

Irshad H. Chaudry, Ph.D.

Dr. Chaudry is the Editor-in-Chief of the journal SHOCK®, a leading research publication that reviews novel therapeutic advances to address shock, trauma, sepsis, inflammation, ischemia, and related pathobiological states, with particular emphasis on the biologic mechanisms that determine the response to such injury. Dr. Chaudry received a B.S. as well as a M.S. with honors from Sind University, and a Ph.D. from Monash University, Australia. After his postdoctoral training at Toronto University, Canada, he was appointed Instructor and subsequently an Assistant Professor at the Jewish Hospital and Washington University School of Medicine. He then moved to Yale University as an Associate Professor and subsequently became a Professor. He moved to Michigan State University in 1986 as Professor and Director of Research and in 1996 became the Director of the Center for Surgical Research at Brown University. In 2000, he became the Director of the Center for Surgical Research at the University of Alabama at Birmingham, and the Vice Chairman of the Department of Surgery. He has over 500 publications to his credit and is a recipient of the NIH MERIT award.

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Larry D. Cowgill, D.V.M., Ph.D.

Dr. Cowgill received his DVM degree from the University of California at Davis and completed his internship and residency training at the University of Pennsylvania. He was a National Institutes of Health Special Research Fellow at the Renal and Electrolyte Section of the University of Pennsylvania School of Medicine and earned a PhD in Comparative Medical Sciences. He is Board Certified in Small Animal Internal Medicine and is Associate Dean for Southern California Clinical Programs, Co-Director of the UC Veterinary Medical Center-San Diego (UCVMC-SD), and Professor in the Department of Medicine and Epidemiology. He oversees the Clinical Nephrology programs and the Companion Animal Hemodialysis Units at the Veterinary Medical Teaching Hospital at Davis and the UCVMC-SD. Dr. Cowgill has more than 35 years of experience in veterinary internal medicine, nephrology, and teaching and has trained many of the leading veterinary nephrologists throughout the world. He is a pioneer in the application of hemodialysis in companion and remains a leading authority in the development of blood purification therapies for renal diseases in animals and people.

Charles J. Fisher, Jr., M.D.

Dr. Fisher, founder and CEO of Margaux Biologics, Inc., is a physician scientist with a distinguished career in both academia and industry spanning over 30 years. Prior to joining industry, Dr. Fisher served as Professor and Head of Critical Care Medicine at The Cleveland Clinic Foundation, and has held professor, division chief and director positions at the University of California at Davis Medical Center, Case Western Reserve University and The Cleveland Clinic Foundation. His research in sepsis, host defense and endothelial dysfunction led to his assisting in the founding of Incyte, and his later recruitment to Eli Lilly & Co, where he led the Xigris (activated Protein C) Global Product Team and successfully registered the first drug approved for the treatment of sepsis. He was recruited to Abbott Laboratories as Vice President for Global Pharmaceutical Development and, among other accomplishments, led the registration of Humira (first fully humanized anti-TNF mab). Other medical firsts include his contributions to the development of, and later approval of, sTNF:fc (Enbrel, 1st soluble anti-TNF tx) and IL-1ra (Kinneret, 1st anti-IL-1 tx). Dr. Fisher has numerous patents and publications to his credit. Prior to founding Margaux Biologics, he was Chief Medical Officer and Executive Vice President of Cardiome Pharma Corp. where he led the team that invented, developed, registered and sold to Merck (\$800M) vernakalant, a novel, first in class, multi-ion channel drug for atrial fibrillation (Brinavess).

Additionally, Dr. Fisher is a decorated, multi tour combat veteran, with extensive military experience in special operations. He is a Life Member of the Special Operations Medical Association, has served as a member of the Defense Science Research Council and on Defense Advanced Research Projects Agency panels, including one focused on universal host defense. His unique background of direct patient care, basic and clinical research, on the ground combat experience, and leadership at all levels, has led to an exemplary track record of building teams, delivering results, medical firsts and saving lives.

Geert Schmid-Schonbein, Ph.D.

Dr. Schmid-Schonbein is Distinguished Professor of Bioengineering, Adjunct Professor in Medicine at the University of California, San Diego (UCSD) and director of the UCSD Microcirculation Laboratory where he and his team are studying organ injury mechanisms, apoptosis in hypertension, and triggers for inflammation in the blood circulation. Dr. Schmid-Schonbein earned his Ph.D. in bioengineering from UCSD in 1976. After a three-year post-doctoral fellowship at Columbia University, he returned to UCSD in 1979 as an assistant professor. Some of Dr. Schmid-Schonbein's early research discoveries involved the behavior of infection-fighting white blood cells. Using engineering techniques, he made the first determination of the force with which white blood cells adhere to the walls of blood vessels as part of the initial process of inflammation. Later, Dr. Schmid-Schonbein concluded that the survival of an acutely ill patient can hinge on the degree to which white blood cells are activated. Recently his group discovered a mechanism that leads to activation of white blood cells, which is due to digestive enzymes and may cause cardiovascular disease. Among his many distinctions, Dr. Schmid-Schonbein is a member of the National Academy of Engineering and a fellow of the American Heart Association. He is a founding fellow of the American Institute for Medical and Biological Engineering, and winner of the Melville Medal from the American Society of Mechanical Engineering.

Cancer Advisory Board

Dr. Radvanyi received his Ph.D. in clinical biochemistry from the University of Toronto. His main research area is tumor immunology studying immune regulation in cancer and identifying new antigens as targets for anti-cancer T-cell therapy. After completing postdoctoral work in Toronto and at Harvard University in Boston at the Joslin Diabetes Center, Dr. Radvanyi joined the Immunology Group at Sanofi-Pasteur in Toronto in 2000 as a Senior Scientist where he helped lead an antigen discovery program that led to the discovery of a group of over-expressed breast cancer-specific genes that are candidates for antigen-specific vaccines against breast cancer. In 2005, Dr. Radvanyi joined the faculty of the University of Texas, MD Anderson Cancer Center, where he also holds the additional appointment as Associate Professor, Department of Breast Medical Oncology, Division of Cancer Medicine.

Involvement in Legal Proceedings

To the best of our knowledge, during the past ten years, none of the following occurred with respect to a present or former director or executive officer of our company: (1) any bankruptcy petition filed by or against such person or any business of which such person was a general partner or executive officer either at the time of the bankruptcy or within two years prior to that time; (2) any conviction in a criminal proceeding or being subject to a pending criminal proceeding (excluding traffic violations and other minor offenses); (3) being subject to any order, judgment or decree, not subsequently reversed, suspended or vacated, of any court of any competent jurisdiction, permanently or temporarily enjoining, barring, suspending or otherwise limiting his involvement in any type of business, securities or

banking activities; (4) being found by a court of competent jurisdiction (in a civil action), the Securities and Exchange Commission or the Commodities Futures Trading Commission to have violated a federal or state securities or commodities law, and the judgment has not been reversed, suspended or vacated; and (5) being the subject of, or a party to, any federal or state judicial or administrative order, judgment, decree or finding, not subsequently reversed, suspended or vacated, relating to an alleged violation of any federal or state securities or commodities law or regulation, law or regulation respecting financial institutions or insurance companies or law or regulation prohibiting mail or wire fraud or fraud in connection with any business entity; or (6) being the subject of, or a party to, any sanction or order, not subsequently reversed, suspended or vacated, of any self-regulatory organization (as defined in Section 3(a)(26) of the Securities Exchange Act of 1934, as amended), any registered entity (as defined in Section 1(a)(29) of the Commodity Exchange Act), or any equivalent exchange, association, entity or organization that has disciplinary authority over its members or associated persons.

EXECUTIVE COMPENSATION

The following executive compensation disclosure reflects all compensation awarded to, earned by or paid to the executive officers below for the fiscal years ended March 31, 2014 and March 31, 2013. The following table summarizes all compensation for fiscal years 2014 and 2013 received by our Chief Executive Officer, and our three most highly compensated executive officers who earned more than \$100,000 in fiscal year 2014.

SUMMARY COMPENSATION TABLE FOR 2014 AND 2013 FISCAL YEARS

NAMED EXECUTIVE OFFICER AND PRINCIPAL POSITION	YEAR	SALARY (\$)	BONUS (\$)	STOCK AWARDS (\$)(5)	OPTION AWARDS (\$)(5)	NON-EQUITY INCENTIVE COMPENSATION (\$)	NON-QUALIFIED DEFERRED COMPENSATION EARNINGS (\$)	ALL OTHER COMP. (\$)	TOTAL (\$)
						PLAN COMPENSATION (\$)	COMPENSATION EARNINGS (\$)	OTHER (\$)	
James A. Joyce (1) CHIEF EXECUTIVE OFFICER	2014	\$330,000	\$70,000	\$ -	\$180,000	\$ -	\$ -	\$ -	\$580,000
	2013	\$325,000	\$12,500	\$ -	\$ -	\$ -	\$ -	\$ -	\$337,500
Richard H. Tullis, PhD (2) VICE PRESIDENT AND CHIEF SCIENCE OFFICER	2014	\$195,000	\$--	\$ -	\$45,000	\$ -	\$ -	\$ -	\$240,000
	2013	\$195,000	\$10,000	\$ -	\$ -	\$ -	\$ -	\$ -	\$205,000
James B. Frakes (3) CHIEF FINANCIAL OFFICER AND SVP-FINANCE	2014	\$180,000	\$3,000	\$ -	\$45,000	\$ -	\$ -	\$ -	\$228,000
	2013	\$180,000	\$7,500	\$ -	\$ -	\$ -	\$ -	\$ -	\$187,500
Rodney S. Kenley (4) PRESIDENT	2014	\$240,000	\$--	\$ -	\$45,000	\$ -	\$ -	\$ -	\$285,000
	2013	\$240,000	\$10,000	\$ -	\$ -	\$ -	\$ -	\$ -	\$250,000

(1) The aggregate number of stock awards and stock option awards issued to Mr. Joyce and outstanding as of March 31, 2014 is 3,400,000 (see share restricted stock grant below) and 14,088,243, respectively. Mr. Joyce received a \$5,000 salary increase from \$325,000 to \$330,000 effective July 1, 2013. In June, 2014, Mr. Joyce received a \$20,000 salary increase from \$330,000 to \$350,000.

Mr. Joyce was granted 4,000,000 shares of restricted common stock, at a price per share of \$0.24, which vested in equal installments over a thirty-six month period that commenced on June 30, 2010. Mr. Joyce has accepted all 4,000,000 shares of the grant and all such shares have vested. Of these shares, Mr. Joyce currently owns 3,400,000 shares.

(2) The aggregate number of stock awards and stock option awards issued to Dr. Tullis and outstanding as of March 31, 2014 is zero and 3,117,175, respectively.

(3) Mr. Frakes was appointed as Chief Financial Officer on September 27, 2010 after previously serving as Senior Vice President-Finance on a part-time basis. The aggregate number of stock awards and stock option awards outstanding as of March 31, 2014 is zero and 1,000,000, respectively. In June 2014, Mr. Frakes received a \$30,000 salary increase from \$180,000 to \$210,000.

(4) Mr. Kenley was appointed President on October 27, 2011. The aggregate number of stock awards and stock option awards issued to Mr. Kenley and outstanding as of March 31, 2014 is zero and 1,500,000, respectively. In June, 2014, Mr. Kenley received a \$20,000 salary increase from \$240,000 to \$260,000.

(5) See note 6 to our financial statements for the years ended March 31, 2014 and 2013 regarding the assumptions made in valuing the stock/option awards in the above table.

Employment Agreements

We entered into an employment agreement with Mr. Joyce effective April 1, 1999. Effective June 1, 2001, Mr. Joyce was appointed President and Chief Executive Officer and his base annual salary was increased from \$120,000 to \$180,000. Effective January 1, 2005, Mr. Joyce's salary was increased from \$180,000 to \$205,000 per year. Under the terms of the agreement, his employment continues at a salary of \$205,000 per year for successive one-year periods, unless given notice of termination 60 days prior to the anniversary of his employment agreement. Effective April 1, 2006, Mr. Joyce's salary was increased from \$205,000 to \$240,000. His salary was subsequently increased to \$265,000 per year and effective May 1, 2008, his salary was increased from \$265,000 to \$290,000 per year. Effective April 1, 2010, his salary was increased from \$290,000 to \$325,000 per year. Effective July 2013, his salary was increased from \$325,000 to \$330,000 per year. In June 2014, his salary was increased from \$330,000 to \$350,000 per year.

During the fiscal year ended March 31, 2014, Mr. Joyce earned a bonus of \$50,000 from us that was paid to him in April 2014 and bonuses of \$20,000 from Exosome Sciences, Inc. All of those bonuses were based upon targets established by our compensation committee.

We entered into an employment agreement with Dr. Tullis effective January 10, 2000. Effective June 1, 2001, Dr. Tullis was appointed our Chief Science Officer. His compensation under the agreement was modified in June 2001 from \$80,000 to \$150,000 per year. Effective January 1, 2005, Dr. Tullis' salary was increased from \$150,000 to \$165,000 per year. Under the terms of the agreement, his employment continues at a salary of \$165,000 per year for successive one-year periods, unless given notice of termination 60 days prior to the anniversary of his employment agreement. Dr. Tullis was granted 250,000 stock options to purchase our common stock in connection the completing certain milestones, such as the initiation and completion of certain clinical trials, the submission of proposals to the U.S. Food and Drug Administration and the filing of a patent application. Effective April 1, 2006, Dr. Tullis' salary was increased to \$180,000 per year. Effective April 1, 2010, his salary was increased from \$180,000 to \$195,000 per year.

Both Mr. Joyce's and Dr. Tullis' agreements provide for medical insurance and disability benefits, one year of severance pay if their employment is terminated by us without cause or due to change in our control before the expiration of their agreements, and allow for bonus compensation and stock option grants as determined by our Board of Directors. Both agreements also contain restrictive covenants preventing competition with us and the use of confidential business information, except in connection with the performance of their duties for us, for a period of two years following the termination of their employment with us.

On September 27, 2010, Mr. Frakes was appointed our Chief Financial Officer. We have not entered into a written employment agreement with Mr. Frakes. As Chief Financial Officer, Mr. Frakes receives an annual salary of \$180,000 and medical insurance benefits. In June 2014, his salary was increased from \$180,000 to \$210,000 per year. During the fiscal year ended March 31, 2014, Mr. Frakes earned a bonus of \$3,000 from Exosome Sciences, Inc. based upon targets established by our compensation committee.

Mr. Kenley was appointed our President on October 27, 2010. Pursuant to a written offer of employment executed by us and Mr. Kenley, he receives an annual salary of \$240,000 and medical insurance benefits. In June 2014, his salary was increased from \$240,000 to \$260,000 per year.

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Outstanding Equity Awards at 2014 Fiscal Year-End

The following table sets forth certain information concerning stock option awards granted to our named executive officers.

OUTSTANDING EQUITY AWARDS AT 2014 FISCAL YEAR END

NAME	OPTIONS AWARDS		EQUITY INCENTIVE PLAN AWARDS NUMBER OF SECURITIES UNDERLYING UNEXERCISED UNEARNED OPTIONS UNEXERCISABLE (#)	OPTION EXERCISE PRICE (\$)	DATE OF OPTION EXPIRATION
	NUMBER OF SECURITIES UNDERLYING UNEXERCISED OPTIONS EXERCISABLE (#)	NUMBER OF SECURITIES UNDERLYING UNEXERCISED OPTIONS UNEXERCISABLE (#)			
James A. Joyce	1,115,550(1)	–	–	\$0.38	02/23/15
	557,775(1)	–	–	\$0.38	02/23/15
	557,775(1)	–	–	\$0.38	02/23/15
	2,857,143(1)	–	–	\$0.21	12/18/15
	2,500,000(2)	–	–	\$0.36	09/21/17
	2,000,000(3)	–	–	\$0.25	02/21/19
	2,500,000(4)	--	–	\$0.25	09/27/20
–(5)	2,000,000	–	\$0.10	07/01/23	
Richard H. Tullis	433,588(6)	–	–	\$0.38	02/23/15
	433,587(6)	–	–	\$0.38	02/23/15
	750,000(7)	–	–	\$0.41	06/14/18
	1,000,000(8)	–	–	\$0.25	09/27/20
	–(5)	500,000	–	\$0.10	07/01/23
James B. Frakes	500,000(9)	–	–	\$0.25	09/27/20
	–(5)	500,000	–	\$0.10	07/01/23
Rodney S. Kenley	854,157(10)	145,843	–	\$0.25	10/27/20
	–(5)	500,000	–	\$0.10	7/01/23

Explanation of Responses:

Note: We have omitted the stock awards columns of the above table because we have no disclosure applicable to those columns.

(1) This option was fully vested as of March 31, 2010 and as a result of the Option Suspension Agreement, the expiration date was extended by 100 days. Subsequent to March 31, 2010, the expiration date of this option was extended to February 23, 2015 (see Item 13 to the Financial Statements).

(2) The option vested 1,000,000 shares at grant, with 500,000 shares vesting each annual anniversary date through June 13, 2010 and as a result of the Option Suspension Agreement, the expiration date was extended by 100 days.

(3) The option vested 1,000,000 at grant, with 500,000 shares vesting on December 31, 2009 and December 31, 2010 and as a result of the Option Suspension Agreement, the expiration date was extended by 100 days.

(4) The option vested 1,000,000 at grant, with 500,000 vesting on each anniversary date through September 27, 2013.

(5) This option vests ratably on July 1, 2014, July 1, 2015 and July 1, 2016.

(6) This option was fully vested as of March 31, 2010. Subsequent to March 31, 2010, the expiration date of this option was extended to February 23, 2015 (see Item 13 to the Financial Statements).

(7) This option was fully vested as of December 15, 2011.

(8) The option was fully vested as of September 27, 2011.

(9) The option was fully vested as of September 27, 2011.

(10) The option vested 250,000 on October 27, 2011 and the remaining 750,000 vests over the 36 months following that date.

We have omitted the stock awards columns of the above table because we have no disclosure applicable to those columns.

Director Compensation for 2014 Fiscal Year

The following director compensation disclosure reflects all compensation awarded to, earned by or paid to the directors below for the fiscal year ended March 31, 2014.

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	Fees Earned or Paid in Cash (\$)	Stock Awards (\$)	Option Awards (\$)	Non-Equity Incentive Plan Compensation (\$)	Nonqualified Deferred Compensation Earnings (\$)	All Other Compensation (\$)	Total (\$)
James A. Joyce (1)	\$-	-	\$-	-	-	-	\$-
Richard H. Tullis (2)	\$-	-	\$-	-	-	-	\$-
Rodney S. Kenley (3)	\$-	-	\$-	-	-	-	\$-
Edward G. Broenniman (4)	\$15,000	-	\$93,902	-	-	-	\$108,902
Franklyn S. Barry, Jr. (5)	\$15,500	-	\$93,902	-	-	-	\$109,402
Chetan S. Shah, MD (6)	\$14,000	-	\$82,725	-	-	-	\$96,725
Phillip A. Ward (7)	\$11,000	-	\$40,244	-	-	-	\$51,244
Thomas V. Wornham (8)	\$10,000	-	\$40,244	-	-	-	\$50,244

(1) All compensation received by Mr. Joyce in fiscal year 2014 is disclosed in the Summary Compensation Table above. Mr. Joyce received no compensation as a director in fiscal year 2014.

(2) All compensation received by Dr. Tullis in fiscal year 2014 is disclosed in the Summary Compensation Table above. Dr. Tullis received no compensation as a director in fiscal year 2014.

(3) All compensation received by Mr. Kenley in fiscal year 2014 is disclosed in the Summary Compensation Table above. Mr. Kenley received no compensation as a director in fiscal year 2014.

(4) The aggregate number of stock awards and options awards issued and outstanding as of March 31, 2014 are 0 and 2,296,080. Mr. Broenniman received a stock option grant of 426,829 shares on March 14, 2014 for his service as an outside director and also received a stock option grant of 460,526 shares on July 24, 2012 for his service as an outside director. The 2014 option vested all 426,829 shares at grant and the 2012 option vested 198,026 at grant, with 262,500 vesting in the June 2013 quarter.

(5) The aggregate number of stock awards and options awards issued and outstanding as of March 31, 2014 are 0 and 2,151,905. Mr. Barry received a stock option grant of 426,829 shares on March 14, 2014 for his service as an outside director and also received a stock option grant of 460,526 shares on July 24, 2012 for his service as an outside director. The 2014 option vested all 426,829 shares at grant and the 2012 option vested 198,026 at grant, with 262,500 vesting in the June 2013 quarter.

(6) The aggregate number of stock awards and options awards issued and outstanding as of March 31, 2014 are 0 and 376,024. Dr. Shah received a stock option grant of 376,024 shares on July 24, 2012 for his service as an outside director. The 2014 option vested all 376,024 shares at grant.

(7) The aggregate number of stock awards and options awards issued and outstanding as of March 31, 2014 are 0 and 555,953. Mr. Ward received a stock option grant of 182,927 shares on March 14, 2014 for his service as an outside director and also received a stock option grant of 373,026 shares on July 24, 2012 for his service as an outside director. The 2014 option vested all 182,927 shares at grant and the 2012 option vested 198,026 at grant, with 175,000 vesting in the June 2013 quarter. Mr. Ward resigned from his position as one of our directors on January 9, 2014.

(8) The aggregate number of stock awards and options awards issued and outstanding as of March 31, 2014 are 0 and 373,026. Mr. Wornham received a stock option grant of 182,927 shares on March 14, 2014 for his service as an outside director and also received a stock option grant of 373,026 shares on July 24, 2012 for his service as an outside director. The 2014 option vested all 182,927 shares at grant and the 2012 option vested 198,026 at grant, with 175,000 vesting in the June 2013 quarter. Mr. Wornham exercised the 2014 stock option in full prior to March 31, 2014. Mr. Wornham resigned from his position as one of our directors on January 9, 2014.

Directors Compensation Program

We maintain a board compensation program, in which only non-employee directors may participate. Please see the “Equity Compensation Plans” section of this prospectus for more information on the program.

SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The following table sets forth information as of December 31, 2014, with respect to the ownership of our common stock, by (i) each person known by us to be the beneficial owner of more than five percent (5%) of the outstanding shares of each class of our capital stock, (ii) each of our directors and director nominees (if any), (iii) each of our named executive officers and (iv) all of our executive officers and directors as a group. The term "executive officer" is defined as the President/Chief Executive Officer, Secretary, Chief Financial Officer/Treasurer, any vice-president in charge of a principal business function (such as administration or finance), or any other person who performs similar policy making functions for us. We believe that each individual or entity named has sole investment and voting power with respect to shares of common stock indicated as beneficially owned by them, subject to community property laws where applicable, excepted where otherwise noted:

TITLE OF CLASS	NAME AND ADDRESS	AMOUNT AND NATURE OF BENEFICIAL OWNERSHIP (1)(2)	PERCENT OF BENEFICIAL OWNERSHIP
Common Stock	James A. Joyce, Chief Executive Officer and Director 9635 Granite Ridge Drive, Suite 100 San Diego, CA 92123	16,888,243 shares (3)	5.0%
Common Stock	Richard H. Tullis, PhD, Chief Scientific Officer and Director 9635 Granite Ridge Drive, Suite 100 San Diego, CA 92123	3,277,592 shares (4)	1.0%
Common Stock	Rodney S. Kenley, President and Director 9635 Granite Ridge Drive, Suite 100 San Diego, CA 92123	1,228,333 shares (5)	*
Common Stock	James B. Frakes, Chief Financial Officer 9635 Granite Ridge Drive, Suite 100 San Diego, CA 92123	718,333 shares (6)	*
Common Stock	Franklyn S. Barry, Jr., Director 9635 Granite Ridge Drive, Suite 100 San Diego, CA 92123	2,257,998 shares (7)	*
Common Stock	Edward G. Broenniman, Director 9635 Granite Ridge Drive, Suite 100 San Diego, CA 92123	2,578,254 shares (8)	*
Common Stock	Chetan Shah, MD, Director (11) 9635 Granite Ridge Drive, Suite 100 San Diego, CA 92123	19,207,084 shares (9)	5.8%
Common Stock	Ellen R Weiner Family Revocable Trust (11) 10645 N. Tatum Blvd., Suite 200-166 Phoenix, AZ 85028	40,510,230 shares (10)	11.8%
Common Stock	Estate of Allen S. Bird 9960 West Cheyenne Avenue, Suite 110 Las Vegas, NV 89129	14,730,620 shares (10)	4.4%
		46,155,837 shares	13.0%

Explanation of Responses:

All Current Directors and Executive Officers as a
Common Stock Group (7 members)

* Less than 1%

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(1) Based on 327,739,188 shares of common stock outstanding on our transfer records as of December 31, 2014.

(2) Calculated pursuant to Rule 13d-3(d)(1) of the Securities Exchange Act of 1934, as amended. Under Rule 13d-3(d)(1), shares not outstanding that are subject to options, warrants, rights or conversion privileges exercisable by a person within 60 days are deemed outstanding for the purpose of calculating the number and percentage owned by such person but not deemed outstanding for the purpose of calculating the percentage owned by each other person listed. Except where otherwise noted, we believe that each individual or entity named has sole investment and voting power with respect to the shares of common stock indicated as beneficially owned by such person, subject to community property laws, where applicable.

(3) Includes 2,231,100 stock options exercisable at \$0.38 per-share, 2,857,143 stock options exercisable at \$0.21 per share, 2,500,000 stock options exercisable at \$0.36 per share, 4,500,000 stock options exercisable at \$0.25 per share, 500,000 stock options exercisable at \$0.10 per share and 500,000 stock options exercisable at \$0.19 per share.

(4) Includes 867,175 stock options exercisable at \$0.38 per share, 750,000 stock options exercisable at \$0.41 per share, 1,000,000 stock options exercisable at \$0.25 per share 125,000 stock options exercisable at \$0.10 per share and 16,667 stock options exercisable at \$0.19 per share.

(5) Includes 1,000,000 stock options exercisable at \$0.25 per share, 125,000 stock options exercisable at \$0.10 per share and 83,333 stock options exercisable at \$0.19 per share.

(6) Includes 500,000 stock options exercisable at \$0.25 per share, 125,000 stock options exercisable at \$0.10 per share and 83,333 stock options exercisable at \$0.19 per share.

(7) Includes 264,550 stock options exercisable at \$0.38 per share, 500,000 stock options exercisable at \$0.41 per share, 500,000 stock options exercisable at \$0.25 per share. 460,526 stock options exercisable at \$0.076 per share and 426,829 stock options exercisable at \$0.082 per share.

(8) Includes 308,725 stock options exercisable at \$0.38 per share, 500,000 stock options exercisable at \$0.41 per share, 600,000 stock options exercisable at \$0.25 per share, 460,526 stock options exercisable at \$0.076 per share and 426,829 stock options exercisable at \$0.082 per share.

(9) Includes warrants to purchase 5,465,983 shares of common stock at exercise prices ranging from \$0.093 per share to \$0.132 per share and 376,024 stock options exercisable at \$0.082 per share.

(10) Includes common stock issuable upon exercise of warrants held by the Ellen R. Weiner Family Revocable Trust and common stock issuable upon exercise of warrants held by the Estate of Allan S. Bird. The trust owns 15,976,643 warrants to purchase common shares at prices ranging from \$0.042 to \$0.108 per share. The estate owns 5,154,916 warrants to purchase common shares at prices ranging from \$0.042 to \$0.108 per share. Mr. Bird was Ms. Weiner's father-in-law. The Ellen R. Weiner Family Trust disclaims any beneficial ownership of the estate's warrants and underlying common stock. The Estate of Mr. Bird disclaims any beneficial ownership of the trust's warrants and underlying common stock.

(11) More-than-5% stockholder.

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CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE

The following describes all transactions since April 1, 2012, and all proposed transactions, in which we were or are to be a participant and the amount involved exceeds the lesser of \$120,000 or one percent of the average of our total assets at year-end for the last two completed fiscal years, and in which any related person had or will have a direct or indirect material interest.

On June 26, 2012, prior to joining our Board of Directors, Mr. Thomas Wornham, now one of our former directors, purchased \$10,000 of units, with each unit consisting of (i) one share of common stock at a price per share of \$0.072 and (ii) a warrant to purchase such number of shares of common stock as shall equal (a) fifty percent of the subscription amount divided by (b) \$0.072 at an exercise price of \$0.107 per share.

On July 24, 2012, our Board of Directors granted, to our four outside directors, ten year options to acquire an aggregate of 1,667,105 shares of our common stock, all with an exercise price of \$0.076 per share.

Between March 2012 and June 2013, Dr. Chetan Shah, one of our directors, participated in several private equity placements with us under which he invested an aggregate amount of \$625,556 and in return received 8.5 million restricted shares of our common stock and seven year warrants to purchase 4,250,000 shares of our common stock.

In June 2013, we borrowed \$80,000 at a 10% interest rate from Mr. Phillip Ward, one of our former directors. We repaid that loan and paid accrued interest of \$133 to Mr. Ward in June 2013.

In July 2013, we borrowed \$400,000 from Mr. Ward and Dr. Shah under 90-day notes bearing 10% interest. If we did not pay back those loans by October 9, 2013, then the notes would bear interest at a penalty rate of 12% and the noteholders would have the right at their discretion (i) to convert their principal and accrued interest into shares of common stock at \$0.088 per share and (ii) receive warrants to purchase common stock equal to 50% of the principal converted under the notes, with an exercise price of \$0.132 per share. We subsequently repaid Mr. Ward's note in cash. That repayment extinguished all potential common stock and warrant issuance provisions of Mr. Ward's note. On July 24, 2014, we issued to Dr. Shah an aggregate of 2,503,966 shares of restricted common stock and a seven-year warrant to issue up to 1,251,983 shares of common stock at an exercise price of \$0.132 per share upon the conversion of an aggregate of \$220,349 of unpaid principal and accrued interest due under his note. The amount converted represented the entire amount outstanding under Dr. Shah's note.

On March 14, 2014, our Board of Directors granted to our three outside directors ten-year options to acquire an aggregate of 1,595,536 shares of our common stock at an exercise price of \$0.082 per share.

On June 6, 2014, our Board of Directors granted to our directors and our Chief Financial Officer ten-year options to acquire an aggregate of 2,602,633 shares of our common stock at an exercise price of \$0.19 per share.

In July 2014, Exosome Sciences, Inc. paid a bonus of \$15,000 to Mr. Joyce.

In October 2014, Exosome Sciences, Inc. paid bonuses of \$15,000 to Mr. Joyce and \$1,500 to Mr. Frakes.

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On October 20, 2014, we issued to Dr. Shah 2,111,111 shares of common stock and three-year warrants to acquire up to 2,111,111 shares of common stock with exercise prices ranging from \$0.093 to \$0.11 per share. The common stock and warrants were issued to Dr. Shah upon his cash exercise, for an aggregate of \$214,000, of previously issued warrants for 2,111,111 shares held by him.

On October 21, 2014 and November 7, 2014, we paid Mr. Franklyn Barry and Mr. Edward Broenniman, two of our outside directors, an aggregate of \$10,944 and \$10,063, respectively, for accrued Board of Directors fees and expenses reimbursable to them. On November 7, 2014, we paid Dr. Tullis \$5,000 for accrued expenses reimbursable to him.

In December 2014, we paid bonuses of \$25,000 to Mr. Joyce, \$15,000 to Mr. Kenley, \$15,000 to Mr. Frakes and \$5,000 to Dr. Tullis.

On December 22, 2014, Exosome Sciences, Inc. paid Mr. Joyce a bonus of \$15,000.

Director Independence

Each of Mr. Barry, Mr. Broenniman and Dr. Shah is an independent director as that term is defined by NASDAQ Stock Market Rule 5605(a)(2). We currently have a compensation and audit committee. Of the members of our Board of Directors, each of Mr. Barry, Mr. Broenniman and Dr. Shah meets the NASDAQ Stock Market's independence standards for members of such committees.

DESCRIPTION OF SECURITIES

General

Our authorized capital consists of 500,000,000 shares of common stock, par value \$0.001 per share. As of December 31, 2014, there were issued and outstanding 327,739,188 shares of common stock.

Common Shares

The holders of our common stock are entitled to one vote (or consent) per share on all matters to be voted on by the stockholders. Holders of common stock are entitled to receive ratably such dividends as may be declared by the Board out of funds legally available therefore. If we liquidate, dissolve or wind up, holders of common stock are entitled to share ratably in all assets remaining after payment of all debts and other liabilities. Holders of common stock have no preemptive, conversion or subscription rights. There are no redemption or sinking fund provisions applicable to the common stock. All outstanding shares of common stock are, and all shares of common stock to be outstanding upon completion of this offering will be, validly issued, fully paid and nonassessable.

Except as otherwise required by Nevada law, all stockholder action is taken by the vote of a majority of common stock voting as a single class present at a meeting of stockholders at which a quorum consisting of a majority of the outstanding shares of common stock is present in person or proxy.

Options and Warrants Convertible into Common Shares

As of December 31, 2014, there were outstanding common share purchase options entitling the holders to purchase 28,956,038 common shares at a weighted average exercise price of \$0.26 per share and warrants entitling the holders to purchase up to 71,794,602 common shares at a weighted average exercise price of \$0.14 per share.

LEGAL MATTERS

The validity of the shares of common stock offered by this prospectus has been passed upon by Raines Feldman LLP. Jennifer A. Post, a partner of the firm, owns approximately 800,000 shares of our common stock.

EXPERTS

The financial statements included in this prospectus as of March 31, 2014 and March 31, 2013 and for each of the years then ended have been audited by Squar, Milner, Peterson, Miranda & Williamson, LLP. Such financial statements have been so included in reliance on the report of such firm, appearing elsewhere herein, given upon their authority as experts in accounting and auditing.

WHERE YOU CAN FIND MORE INFORMATION

We are a reporting company under the Securities Exchange Act of 1934, as amended, and we file annual, quarterly and current reports and other information with the Securities and Exchange Commission. The public may read and copy any materials that we file with the Securities and Exchange Commission at its Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. The public may obtain information on the operation of the Public Reference Room by calling the Securities and Exchange Commission at 1-800-SEC-0330. The Securities and Exchange Commission maintains an Internet site at <http://www.sec.gov> that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the Securities and Exchange Commission.

Our website address is www.aethlonmedical.com. Our website and the information contained on our website are not incorporated into this prospectus or the registration statement of which it forms a part.

DISCLOSURE OF COMMISSION POSITION ON INDEMNIFICATION FOR SECURITIES ACT LIABILITIES

Nevada Law.

We are incorporated in Nevada. Subsection 1 of Section 78.7502 of the Nevada Revised Statutes empowers a corporation to indemnify any person who was or is a party or is threatened to be made a party to any threatened,

pending or completed action, suit or proceeding, whether civil, criminal, administrative or investigative (other than an action by or in the right of the corporation) by reason of the fact that he is or was a director, officer, employee or agent of the corporation, or is or was serving at the request of the corporation as a director, officer, employee or agent of another corporation or other enterprise, against expenses (including attorneys' fees), judgments, fines and amounts paid in settlement actually and reasonably incurred by him in connection with such action, suit or proceeding if he is not liable pursuant to Section 78.138 of the Nevada Revised Statutes or if he acted in good faith and in a manner he reasonably believed to be in or not opposed to the best interests of the corporation, and, with respect to any criminal action or proceeding, had no reasonable cause to believe his conduct was unlawful. Subsection 7 of Section 78.138 provides that, with certain exceptions, a director or officer is not individually liable to the corporation or its stockholders or creditors for any damages as a result of any act or failure to act in his capacity as a director or officer unless it is proven that (i) his act or failure to act constituted a breach of his fiduciary duties as a director or officer, and (ii) his breach of those duties involved intentional misconduct, fraud or a knowing violation of the law.

Subsection 2 of Section 78.7502 empowers a corporation to indemnify any person who was or is a party or is threatened to be made a party to any threatened, pending or completed action or suit by or in the right of the corporation to procure a judgment in its favor by reason of the fact that such person acted in any of the capacities set forth above against expenses, including amounts paid in settlement and attorneys' fees actually and reasonably incurred by him in connection with the defense or settlement of such action or suit if he acted under similar standards, except that no indemnification may be made in respect of any claim, issue or matter as to which such person shall have been adjudged by a court of competent jurisdiction to be liable to the corporation or for amounts paid in settlement to the corporation, unless and only to the extent that the court in which such action or suit was brought or other court of competent jurisdiction determines that, in view of all the circumstances of the case, such person is fairly and reasonably entitled to indemnity for such expenses as the court deems proper.

Section 78.7502 further provides that to the extent a director or officer of a corporation has been successful in the defense of any action, suit or proceeding referred to in subsections (1) and (2) thereof, or in the defense of any claim, issue or matter therein, he shall be indemnified against expenses (including attorneys' fees) actually and reasonably incurred by him in connection therewith. Subsection 3 of Section 78.751 of the Nevada Revised Statutes provides that the indemnification provided for by Section 78.7502 shall not be deemed exclusive or exclude any other rights to which the indemnified party may be entitled (except that indemnification will generally not be available to a person if a final adjudication establishes that his acts or omissions involved intentional misconduct, fraud or a knowing violation of the law and were material to the cause of action) and that the indemnification shall continue as to directors, officers, employees or agents who have ceased to hold such positions, and to their heirs, executors and administrators. Section 78.752 empowers the corporation to purchase and maintain insurance on behalf of a director, officer, employee or agent of the corporation against any liability asserted against him or incurred by him in any such capacity or arising out of his status as such whether or not the corporation would have the power to indemnify him against such liabilities under Section 78.7502.

By-Laws.

Our by-laws provide for the elimination of the personal liability of our officers, directors, corporate employees and agents to the fullest extent permitted by the provisions of the Nevada Law. Under such provisions, we shall indemnify a director or officer (and may indemnify a corporate employee or agent) who in his capacity as such is made, or threatened to be made, party to any suit or proceeding, if it is determined that such person acted in good faith and in a manner he reasonably believed to be in or not opposed to the best interests of our company and, with respect to any criminal action or proceeding, had no reasonable cause to believe his conduct was unlawful.

Liability Insurance.

We maintain directors' and officers' liability insurance covering our directors and officers against expenses and liabilities arising from certain actions to which they may become subject by reason of having served in such role, including insurance for claims against these persons brought under securities laws. Such insurance is subject to the coverage amounts, exceptions, deductibles and other conditions set forth in the policy as in effect at the time of a

claim, if any. There is no assurance that we will maintain liability insurance for our directors and officers.

Public Policy Limitations.

Insofar as indemnification for liabilities arising under the Securities Act of 1933, as amended, may be permitted to our directors, officers and controlling persons pursuant to the foregoing provisions, or otherwise, we have been advised that in the opinion of the Securities and Exchange Commission such indemnification is against public policy as expressed in the Securities Act of 1933, as amended, and is, therefore, unenforceable. In the event that a claim for indemnification against such liabilities (other than the payment by us of expenses incurred or paid by one of our directors, officers or controlling persons in the successful defense of any action, suit or proceeding) is asserted by such director, officer or controlling person in connection with the securities being registered, we will, unless in the opinion of our counsel the matter has been settled by controlling precedent, submit to a court of appropriate jurisdiction the question whether such indemnification by us is against public policy as expressed in the Securities Act of 1933, as amended, and will be governed by the final adjudication of such issue.

AETHLON MEDICAL, INC. AND SUBSIDIARY

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders

Aethlon Medical, Inc. and Subsidiary

We have audited the accompanying consolidated balance sheets of Aethlon Medical, Inc. and Subsidiary (the "Company") as of March 31, 2014 and 2013 and the related consolidated statements of operations, deficit and cash flows for each of the years in the two-year period ended March 31, 2014. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Aethlon Medical, Inc. and Subsidiary as of March 31, 2014 and 2013 and the consolidated results of their operations and cash flows for each of the years in the two-year period ended March 31, 2014 in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1, the accompanying consolidated financial statements have been prepared assuming that the Company will continue as a going concern. The Company has incurred continuing losses from operations and at March 31, 2014 is in default on certain debt agreements, has negative working capital of approximately \$14,169,000 and an accumulated deficit of approximately \$74,833,000. A significant 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. These conditions, among others, raise substantial doubt about the Company's ability to continue as a going concern. Management's plans regarding these matters are also described in Note 1. The accompanying consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

Subsequent to March 31, 2014, as more fully discussed in Note 16, the Company entered into amended debt agreements with certain creditors which resulted in conversion of debt into common stock and the elimination of warrant and convertible debt price protection features. As a result, derivative liabilities of approximately \$10,679,000 were reclassified to equity and certain debt holders converted their debt and accrued interest into equity in the approximate amount of \$1,235,000. Due to the significance of such subsequent events, the Company has included an unaudited pro forma balance sheet as of March 31, 2014 alongside its consolidated balance sheets to present the effect of these subsequent events as if they had occurred on March 31, 2014.

/s/ SQUAR, MILNER, PETERSON, MIRANDA & WILLIAMSON, LLP

NEWPORT BEACH, CALIFORNIA

JULY 14, 2014

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AETHLON MEDICAL, INC. AND SUBSIDIARY

CONSOLIDATED BALANCE SHEETS

	March 31, 2014	March 31, 2013	Pro Forma March 31, 2014 (Note 16) (unaudited)
ASSETS			
CURRENT ASSETS			
Cash	\$1,250,279	\$125,274	\$1,250,279
Accounts receivable	95,177	208,781	95,177
Deferred financing costs	83,191	863	83,191
Prepaid expenses	50,699	29,602	50,699
TOTAL CURRENT ASSETS	1,479,346	364,520	1,479,346
NON-CURRENT ASSETS			
Property and equipment, net	84,279	145	84,279
Patents, net	112,489	121,653	112,489
Deposits	18,988	10,376	18,988
TOTAL NON-CURRENT ASSETS	215,756	132,174	215,756
TOTAL ASSETS	\$1,695,102	\$496,694	\$1,695,102
LIABILITIES AND DEFICIT			
CURRENT LIABILITIES			
Accounts payable	\$517,651	\$822,832	\$517,651
Due to related parties	839,070	736,070	839,070
Notes payable	390,000	321,381	390,000
Convertible notes payable, current portion	1,367,655	2,367,631	482,655
Derivative liabilities	10,679,067	3,588,239	–
Other current liabilities	1,855,374	1,804,985	1,280,124
TOTAL CURRENT LIABILITIES	15,648,817	9,641,138	3,509,500
NONCURRENT LIABILITIES			
Convertible notes payable, noncurrent portion	776,451	–	1,001,451
TOTAL NONCURRENT LIABILITIES	776,451	–	1,001,451
TOTAL LIABILITIES	16,425,268	9,641,138	4,510,951

COMMITMENTS AND CONTINGENCIES (Note 13)

STOCKHOLDERS' DEFICIT

Explanation of Responses:

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Common stock, \$0.001 par value, 500,000,000 and 250,000,000 shares authorized at March 31, 2014 and 2013, respectively; 224,973,980 and 173,674,201 issued and outstanding at March 31, 2014 and 2013, respectively	224,984	173,685	250,994
Additional paid-in capital	59,659,137	52,157,196	74,116,754
Accumulated deficit	(74,832,557)	(61,475,325)	(77,401,867)
TOTAL AETHLON MEDICAL, INC STOCKHOLDERS' DEFICIT	(14,948,436)	(9,144,444)	(3,034,119)
NONCONTROLLING INTERESTS	218,270	–	218,270
TOTAL DEFICIT	(14,730,166)	(9,144,444)	(2,815,849)
TOTAL LIABILITIES AND DEFICIT	\$1,695,102	\$496,694	\$1,695,102

See accompanying notes to the consolidated financial statements.

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AETHLON MEDICAL, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF OPERATIONS

FOR THE YEARS ENDED MARCH 31, 2014 AND 2013

	Years Ended March 31,	
	2014	2013
REVENUES:		
Government contract revenue	\$1,623,769	\$1,230,004
Total revenues	1,623,769	1,230,004
OPERATING EXPENSES		
Professional fees	1,521,397	1,892,270
Payroll and related	2,227,194	2,166,989
General and administrative	931,106	746,099
	4,679,697	4,805,358
OPERATING LOSS	(3,055,928)	(3,575,354)
OTHER (INCOME) EXPENSE		
Loss on debt conversion	40,257	139,839
Change in fair value of derivative liabilities	8,547,015	44,705
Loss on litigation settlement	583,601	–
Other expenses	(75,060)	(172)
Interest and other debt expenses	1,287,221	1,132,314
	10,383,034	1,316,686
NET LOSS BEFORE NONCONTROLLING INTERESTS	(13,438,962)	(4,892,040)
LOSS ATTRIBUTABLE TO NONCONTROLLING INTERESTS	(81,730)	–
LOSS ATTRIBUTABLE TO COMMON STOCKHOLDERS	\$(13,357,232)	\$(4,892,040)
Basic and diluted net loss per share available to common stockholders	\$(0.07)	\$(0.03)
Weighted average number of common shares outstanding - basic and diluted	194,058,972	149,223,601

See accompanying notes to the consolidated financial statements.

AETHLON MEDICAL, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF DEFICIT

FOR THE YEARS ENDED MARCH 31, 2014 AND 2013

	ATTRIBUTABLE TO AETHLON MEDICAL, INC.					NON- CONTROLLING INTERESTS	TOTAL DEFICIT
	COMMON STOCK SHARES	AMOUNT	ADDITIONAL PAID IN CAPITAL	ACCUMULATED DEFICIT			
BALANCE - MARCH 31, 2012	117,515,892	\$ 117,518	\$ 47,170,146	\$ (56,583,285)	\$	–	\$(9,295,621)
Issuance of common stock for cash	29,724,545	29,726	2,080,108	–	–	–	2,109,834
Issuances of common stock upon conversions of notes payable	21,941,154	21,941	1,673,118	–	–	–	1,695,059
Issuance of common stock for services	2,896,181	2,896	256,139	–	–	–	259,035
Patent license fees paid with issuance of common stock	246,429	246	17,004	–	–	–	17,250
Reclassification of derivative liability into equity	–	–	45,081	–	–	–	45,081
Issuance of common stock for interest	116,000	120	11,726	–	–	–	11,846
Loss on debt conversion	1,234,000	1,238	138,601	–	–	–	139,839
Stock-based compensation expense	–	–	765,273	–	–	–	765,273
Net loss	–	–	–	(4,892,040)	–	–	(4,892,040)
BALANCE - MARCH 31, 2013	173,674,201	\$ 173,685	\$ 52,157,196	\$ (61,475,325)	\$	–	\$(9,144,444)

See accompanying notes to the consolidated financial statements.

Explanation of Responses:

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AETHLON MEDICAL, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF DEFICIT

FOR THE YEARS ENDED MARCH 31, 2014 AND 2013

	ATTRIBUTABLE TO AETHLON MEDICAL, INC.					NON- CONTROLLING INTERESTS	TOTAL DEFICIT
	COMMON STOCK SHARES	AMOUNT	ADDITIONAL PAID IN CAPITAL	ACCUMULATED DEFICIT			
BALANCE - MARCH 31, 2013	173,674,201	\$ 173,685	\$ 52,157,196	\$ (61,475,325)	\$ -	\$ (9,144,444)	
Issuances of common stock upon conversions of notes payable	10,574,024	10,572	716,204	-	-	726,776	
Issuance of common stock for cash - Aethlon	16,872,739	16,873	1,660,159	-	-	1,677,032	
Issuance of common stock for cash - ESI	-	-	1,200,000	-	300,000	1,500,000	
Issuance of common stock for services	3,071,150	3,071	389,022	-	-	392,093	
Issuance of common stock under convertible debt restructuring	4,507,105	4,507	851,842	-	-	856,349	
Issuance of common stock under stock option exercises for accrued expenses	158,536	159	12,841	-	-	13,000	
Reclassification of derivative liability into equity	-	-	1,456,187	-	-	1,456,187	
Issuance of common stock under cashless warrant exercises	12,716,225	12,717	(12,717)	-	-	-	
Shares issued under restricted stock grant	3,400,000	3,400	(3,400)	-	-	-	

Explanation of Responses:

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Issuance of common stock on litigation settlement	–	–	583,601	–	–	583,601
Loss on debt conversion	–	–	40,256	–	–	40,256
Stock-based compensation expense	–	–	607,946	–	–	607,946
Net loss	–	–	–	(13,357,232)	(81,730)	(13,438,962)
BALANCE - MARCH 31, 2014	224,973,980	\$ 224,984	\$ 59,659,137	\$ (74,832,557)	\$ 218,270	\$(14,730,166)

See accompanying notes to the consolidated financial statements.

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AETHLON MEDICAL, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE YEARS ENDED MARCH 31, 2014 AND 2013

	2014	2013
Cash flows from operating activities:		
Net loss	\$(13,438,962)	\$(4,892,040)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	21,087	10,484
Debt restructuring cost	856,349	139,839
Non-cash interest expense	-	11,846
Loss on litigation settlement	583,601	-
Change in estimated fair value of derivative liabilities	8,547,015	44,705
Loss on debt conversion	40,256	-
Fair market value of equity instruments issued for services	392,093	259,035
Stock based compensation	607,946	765,273
Patent license fees paid with issuance of common stock	-	17,250
Amortization of debt discount and deferred financing costs	5,147	594,358
Changes in operating assets and liabilities:		
Accounts receivable	113,604	191,333
Prepaid expenses	(21,097)	1,850
Other assets	(8,612)	-
Accounts payable and other current liabilities	46,602	751,210
Due to related parties	116,000	6,000
Net cash used in operating activities	(2,138,971)	(2,098,857)
Cash flows from investing activities:		
Purchases of property and equipment	(96,056)	-
Net cash used in investing activities	(96,056)	-

See accompanying notes to the consolidated financial statements.

AETHLON MEDICAL, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE YEARS ENDED MARCH 31, 2014 AND 2013

	2014	2013
Cash flows from financing activities:		
Principal repayments of notes payable	(217,000)	(29,610)
Proceeds from the issuance of notes payable	400,000	-
Net proceeds from the issuance of common stock	3,177,032	2,109,834
Net cash provided by financing activities	3,360,032	2,080,224
Net increase (decrease) in cash	1,125,005	(18,633)
Cash at beginning of year	125,274	143,907
Cash at end of year	\$1,250,279	\$125,274
Supplemental disclosure of cash flow information - Cash paid during the year for:		
Interest	\$13,950	\$2,821
Income taxes	\$-	\$-
Supplement information for non-cash investing and financing activities:		
Conversion of debt, accrued liabilities and accrued interest to common stock	\$726,776	\$1,695,059
Reclassification of accounts payable to convertible notes payable	\$47,000	\$-
Reclassification of accrued interest to convertible notes payable	\$20,027	\$-
Recording deferred financing costs associated with notes payable and convertible notes payable	\$83,191	\$7,500
Reclassification of warrant derivative liability into equity	\$1,456,187	\$45,081
Issuance of shares under cashless warrant exercises	\$12,717	\$-
Exercise of stock option for accrued expenses	\$13,000	\$-
Reclassification of note payable to convertible notes payable	\$-	\$75,000
Stock issued under restricted stock grant	\$3,400	\$-

See accompanying notes to the consolidated financial statements.

AETHLON MEDICAL, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

MARCH 31, 2014 AND 2013

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

ORGANIZATION

Aethlon Medical, Inc. and subsidiary ("Aethlon", the "Company", "we" or "us") is a medical device company focused on creating innovative devices that address unmet medical needs in cancer, infectious disease and other life-threatening conditions. At the core of our developments is the Aethlon ADAPT™ (Adaptive Dialysis-Like Affinity Platform Technology) system, a medical device platform that converges single or multiple affinity drug agents with advanced plasma membrane technology to create therapeutic filtration devices that selectively remove harmful particles from the entire circulatory system without loss of essential blood components. On June 25, 2013, the United States Food and Drug Administration (FDA) approved an Investigational Device Exemption (IDE) that allows us to initiate human feasibility studies of the Aethlon Hemopurifier® in the United States. Under the feasibility study protocol, we will enroll ten end-stage renal disease patients who are infected with the Hepatitis C virus (HCV) to demonstrate the safety of Hemopurifier therapy. Successful completion of this study will allow us the opportunity to initiate pivotal studies that are required for market clearance to treat HCV and other disease conditions in the United States.

Successful outcomes of human trials will also be required by the regulatory agencies of certain foreign countries where we intend to sell this device. Some of our patents may expire before FDA approval or approval in a foreign country, if any, is obtained. However, we believe that certain patent applications and/or other patents issued more recently will help protect the proprietary nature of the Hemopurifier(R) treatment technology.

In October 2013, our subsidiary, Exosome Sciences, Inc. ("ESI"), commenced operations with a focus on advancing exosome-based strategies to diagnose and monitor the progression of cancer, infectious disease and other life-threatening conditions.

Our common stock is quoted on the OTCQB marketplace administered by the OTC Markets Group under the symbol "AEMD."

UNAUDITED PRO FORMA BALANCE SHEET INFORMATION

During June and July 2014, we entered into agreements with two existing convertible note holders to convert one note into common stock and to extend the second note and to restructure warrants related to the original note issuances removing certain price protection features from such warrants. The transaction resulted in not only the conversion of debt to equity but also the reclassification of such warrants from derivative liabilities to equity. As further explained in Note 16, we have presented an unaudited March 31, 2014 pro forma balance sheet to reflect such transactions as if they had occurred on March 31, 2014.

PRINCIPLES OF CONSOLIDATION

The accompanying consolidated financial statements include the accounts of Aethlon Medical, Inc. and its majority-owned and controlled subsidiary, ESI. All significant intercompany balances and transactions have been eliminated in consolidation. The Company classifies the noncontrolling interests in ESI as part of consolidated net loss in the fiscal year ended March 31, 2014 and includes the accumulated amount of noncontrolling interests as part of stockholders' equity. For the fiscal year ended March 31, 2013, ESI was a wholly-owned subsidiary. During the fiscal year ended March 31, 2014, Aethlon Medical, Inc. reduced its ownership percentage to 80% by ESI's issuance of 300,000 shares of ESI common stock in exchange for cash of \$1,500,000.

The losses at ESI during the fiscal year ended March 31, 2014 reduced the noncontrolling interests on our consolidated balance sheet by \$81,730 from \$300,000 to \$218,270 at March 31, 2014.

GOING CONCERN

The accompanying consolidated financial statements have been prepared assuming that we will continue as a going concern, which contemplates, among other things, the realization of assets and satisfaction of liabilities in the ordinary course of business. We have incurred continuing losses from operations and at March 31, 2014 are in default on certain debt agreements, have negative working capital of approximately \$14,169,000, and an accumulated deficit of approximately \$74,833,000. These factors, among other matters, raise substantial doubt about our ability to continue as a going concern. A significant amount of additional capital will be necessary to advance the development of our products to the point at which they may become commercially viable. We intend to fund operations, working capital and other cash requirements for the fiscal year ending March 31, 2015 through debt and/or equity financing arrangements as well as through revenues and related cash receipts under our government contracts (see Note 11).

We are currently addressing our liquidity issue by seeking additional investment capital through private placements of common stock and debt and by applying for additional grants issued by government agencies in the United States. We believe that our cash on hand and funds expected to be received from additional private investment will be sufficient

to meet our liquidity needs for fiscal 2015. However, no assurance can be given that we will receive any funds in addition to the funds we have received to date.

The successful outcome of future activities cannot be determined at this time and there is no assurance that, if achieved, we will have sufficient funds to execute our intended business plan or generate positive operating results.

Subsequent to March 31, 2014, we completed several significant transactions related to our convertible notes (see Note 16).

The consolidated financial statements do not include any adjustments related to this uncertainty and as to the recoverability and classification of asset carrying amounts or the amount and classification of liabilities that might result should the Company be unable to continue as a going concern.

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AETHLON MEDICAL, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

MARCH 31, 2014 AND 2013

RISKS AND UNCERTAINTIES

We operate in an industry that is subject to intense competition, government regulation and rapid technological change. Our operations are subject to significant risk and uncertainties including financial, operational, technological, regulatory, and including the potential risk of business failure.

USE OF ESTIMATES

We prepare our consolidated financial statements in conformity with GAAP, which requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and reported amounts of revenues and expenses during the reporting periods. Significant estimates made by management include, among others, realization of long-lived assets, valuation of derivative liabilities, estimating fair value associated with debt and equity transactions and valuation of deferred tax assets. Actual results could differ from those estimates.

CASH AND CASH EQUIVALENTS

Accounting standards define "cash and cash equivalents" as any short-term, highly liquid investment that is both readily convertible to known amounts of cash and so near their maturity that they present insignificant risk of changes in value because of changes in interest rates. For the purpose of financial statement presentation, we consider all highly liquid investment instruments with original maturities of three months or less when purchased, or any investment redeemable without penalty or loss of interest to be cash equivalents. As of March 31, 2014 and 2013, we had no assets that were classified as cash equivalents.

FAIR VALUE OF FINANCIAL INSTRUMENTS

The carrying amount of our cash, accounts receivable, accounts payable, and other current liabilities approximates their estimated fair values due to the short-term maturities of those financial instruments. The carrying amount of the notes payable approximates their fair value due to the short maturity of the notes and since the interest rates approximate current market interest rates for similar instruments. Derivative liabilities recorded in connection with warrants and embedded conversion features of certain convertible notes payable are reported at their estimated fair value, with changes in fair value being reported in results of operations (see Note 10).

Management has concluded that it is not practical to determine the estimated fair value of amounts due to related parties because the transactions cannot be assumed to have been consummated at arm's length, the terms are not deemed to be market terms, there are no quoted values available for these instruments, and an independent valuation would not be practicable due to the lack of data regarding similar instruments, if any, and the associated potential costs.

Other than our derivative liabilities, we do not have any assets or liabilities that are measured at fair value on a recurring basis and, during the years ended March 31, 2014 and 2013, did not have any assets or liabilities that were measured at fair value on a nonrecurring basis except as described in Note 10 under derivative liabilities.

CONCENTRATIONS OF CREDIT RISKS

Cash is maintained at two financial institutions in checking accounts and related cash management accounts. Accounts at these institutions are secured by the Federal Deposit Insurance Corporation ("FDIC") up to \$250,000. Our March 31, 2014 cash balances were approximately \$1,000,000 over such insured amount. We do not believe that the Company is exposed to any significant risk with respect to its cash.

All of our accounts receivable at March 31, 2014 and 2013 and all of our revenue in the fiscal years ended March 31, 2014 and 2013 were directly from the U.S. Department of Defense or from a subcontract under Battelle, which is a prime contractor with the U.S. Department of Defense.

PROPERTY AND EQUIPMENT

Property and equipment are stated at cost. Depreciation is computed using the straight-line method over the estimated useful lives of the related assets, which range from two to five years. Repairs and maintenance are charged to expense as incurred while improvements are capitalized. Upon the sale or retirement of property and equipment, the accounts are relieved of the cost and the related accumulated depreciation with any gain or loss included in the consolidated statements of operations.

INCOME TAXES

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to the difference between the consolidated financial statements and their respective tax basis. Deferred income taxes reflect the net tax effects of (a) temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts reported for income tax purposes, and (b) tax credit carryforwards. We record a valuation allowance for deferred tax assets when, based on our best estimate of taxable income (if any) in the foreseeable future, it is more likely than not that some portion of the deferred tax assets may not be realized.

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AETHLON MEDICAL, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

MARCH 31, 2014 AND 2013

LONG-LIVED ASSETS

Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that their carrying amounts may not be recoverable. If the cost basis of a long-lived asset is greater than the projected future undiscounted net cash flows from such asset, an impairment loss is recognized. We believe no impairment charges were necessary during the fiscal years ended March 31, 2014 and 2013.

LOSS PER SHARE

Basic loss per share is computed by dividing net income available to common stockholders by the weighted average number of common shares outstanding during the period of computation. Diluted loss per share is computed similar to basic loss per share except that the denominator is increased to include the number of additional common shares that would have been outstanding if potential common shares had been issued, if such additional common shares were dilutive. Since we had net losses for all periods presented, basic and diluted loss per share are the same, and additional potential common shares have been excluded as their effect would be antidilutive.

As of March 31, 2014 and 2013, a total of 143,074,602 and 142,701,202 potential common shares, consisting of shares underlying outstanding stock options, warrants and convertible notes payable were excluded as their inclusion would be antidilutive.

SEGMENTS

Historically, we operated in one segment that was based on our development of therapeutic devices. However in the December 2013 quarter, we initiated the operations of ESI to develop diagnostic tests. As a result, we now operate in two segments, Aethlon for therapeutic applications and ESI for diagnostic applications (See Note 14).

DEFERRED FINANCING COSTS

Costs related to the issuance of debt are capitalized and amortized to interest expense over the life of the related debt using the effective interest method. We recorded amortization expense related to our deferred offering costs of \$863 and \$127,200 during the fiscal years ended March 31, 2014 and 2013, respectively.

REVENUE RECOGNITION

DARPA Contract -- With respect to revenue recognition, we entered into a government contract with DARPA and have recognized revenue of \$1,466,482 and \$1,230,004 under that contract during the fiscal years ended March 31, 2014 and 2013, respectively. We adopted the Milestone method of revenue recognition for the DARPA contract under ASC 605-28 "Revenue Recognition – Milestone Method" and we believe we meet the requirements under ASC 605-28 for reporting contract revenue under the Milestone Method for the fiscal years ended March 31, 2014 and 2013.

In order to account for this contract, we identify the deliverables included within the contract and evaluate which deliverables represent separate units of accounting based on if certain criteria are met, including whether the delivered element has standalone value to the collaborator. The consideration received is allocated among the separate units of accounting, and the applicable revenue recognition criteria are applied to each of the separate units.

A milestone is an event having all of the following characteristics:

- (1) There is substantive uncertainty at the date the arrangement is entered into that the event will be achieved. A vendor's assessment that it expects to achieve a milestone does not necessarily mean that there is not substantive uncertainty associated with achieving the milestone.
- (2) The event can only be achieved based in whole or in part on either: (a) the vendor's performance; or (b) a specific outcome resulting from the vendor's performance.
- (3) If achieved, the event would result in additional payments being due to the vendor.

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AETHLON MEDICAL, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

MARCH 31, 2014 AND 2013

A milestone does not include events for which the occurrence is either: (a) contingent solely upon the passage of time; or (b) the result of a counterparty's performance.

The policy for recognizing deliverable consideration contingent upon achievement of a milestone must be applied consistently to similar deliverables.

The assessment of whether a milestone is substantive is performed at the inception of the arrangement. The consideration earned from the achievement of a milestone must meet all of the following for the milestone to be considered substantive:

(1) The consideration is commensurate with either: (a) the vendor's performance to achieve the milestone; or (b) the enhancement of the value of the delivered item or items as a result of a specific outcome resulting from the vendor's performance to achieve the milestone;

(2) The consideration relates solely to past performance; and

(3) The consideration is reasonable relative to all of the deliverables and payment terms (including other potential milestone consideration) within the arrangement.

A milestone is not considered substantive if any portion of the associated milestone consideration relates to the remaining deliverables in the unit of accounting (i.e., it does not relate solely to past performance). To recognize the milestone consideration in its entirety as revenue in the period in which the milestone is achieved, the milestone must be substantive in its entirety. Milestone consideration cannot be bifurcated into substantive and nonsubstantive components. In addition, if a portion of the consideration earned from achieving a milestone may be refunded or adjusted based on future performance, the related milestone is not considered substantive.

See Note 11 for the additional disclosure information required under ASC 605-28.

Battelle Subcontract -- We entered into a subcontract agreement with Battelle Memorial Institute (“Battelle”) in March 2013. Battelle was chosen by DARPA to be the prime contractor on the systems integration portion of the original DARPA contract and we are one of several subcontractors on that systems integration project. The Battelle subcontract is cost-reimbursable under a time and materials basis. We began generating revenues under the subcontract during the three months ended September 30, 2013 and for the fiscal year 2014 recorded revenue of \$157,287.

Our revenue under this contract is a function of cost reimbursement plus an overhead mark-up for hours devoted to the project by specific employees (with specific hourly rates for those employees). Battelle engages us as needed. Each payment requires approval by the program manager at Battelle.

STOCK-BASED COMPENSATION

Employee stock options and rights to purchase shares under stock participation plans are accounted for under the fair value method. Accordingly, share-based compensation is measured when all granting activities have been completed, generally the grant date, based on the fair value of the award. The exercise price of options is generally equal to the market price of the Company's common stock (defined as the closing price as quoted on the OTCBB on the date of grant). Compensation cost recognized by the Company includes (a) compensation cost for all equity incentive awards granted prior to April 1, 2006, but not yet vested, based on the grant-date fair value estimated in accordance with the original provisions of the then current accounting standards, and (b) compensation cost for all equity incentive awards granted subsequent to April 1, 2006, based on the grant-date fair value estimated in accordance with the provisions of subsequent accounting standards. We use a Binomial Lattice option pricing model for estimating fair value of options granted (see Note 6).

The following table summarizes share-based compensation expenses relating to shares and options granted and the effect on loss per common share during the years ended March 31, 2014 and 2013:

	March 31, 2014	March 31, 2013
Vesting of Stock Options	\$541,588	\$355,578
Incremental fair value of option Modifications	1,914	23,028
Vesting Expense Associated with CEO Restricted Stock Grant	64,444	386,667
Total Stock-Based Compensation Expense	\$607,946	\$765,273
Basic and diluted loss per common share	\$(0.00)	\$(0.01)

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AETHLON MEDICAL, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

MARCH 31, 2014 AND 2013

We account for transactions involving services provided by third parties where we issue equity instruments as part of the total consideration using the fair value of the consideration received (i.e. the value of the goods or services) or the fair value of the equity instruments issued, whichever is more reliably measurable. In transactions, when the value of the goods and/or services are not readily determinable and (1) the fair value of the equity instruments is more reliably measurable and (2) the counterparty receives equity instruments in full or partial settlement of the transactions, we use the following methodology:

a) For transactions where goods have already been delivered or services rendered, the equity instruments are issued on or about the date the performance is complete (and valued on the date of issuance).

b) For transactions where the instruments are issued on a fully vested, non-forfeitable basis, the equity instruments are valued on or about the date of the contract.

c) For any transactions not meeting the criteria in (a) or (b) above, we re-measure the consideration at each reporting date based on its then current stock value.

We review share-based compensation on a quarterly basis for changes to the estimate of expected award forfeitures based on actual forfeiture experience. The effect of adjusting the forfeiture rate for all expense amortization after March 31, 2006 is recognized in the period the forfeiture estimate is changed. The effect of forfeiture adjustments for the fiscal year ended March 31, 2014 was insignificant.

PATENTS

Patents include both foreign and domestic patents. There were several patents pending at March 31, 2014. We capitalize the cost of patents and patents pending, some of which were acquired, and amortize such costs over the shorter of the remaining legal life or their estimated economic life, upon issuance of the patent. The unamortized costs of patents and patents pending are subject to our review for impairment under our long-lived asset policy above.

STOCK PURCHASE WARRANTS

We grant warrants in connection with the issuance of convertible notes payable and the issuance of common stock for cash. When such warrants are classified as equity and issued in connection with debt, we measure the relative estimated fair value of such warrants and record it as a discount from the face amount of the convertible notes payable. Such discounts are amortized to interest expense over the term of the notes using the effective interest method. Warrants issued in connection with common stock for cash, if classified as equity, are considered issued in connection with equity transactions and the warrant fair value is recorded to additional paid-in-capital. Lastly, warrants not meeting equity classification are recorded as derivative instruments.

DERIVATIVE INSTRUMENTS

We evaluate free-standing derivative instruments (or embedded derivatives) to properly classify such instruments within equity or as liabilities in our financial statements. Our policy is to settle instruments indexed to our common shares on a first-in-first-out basis.

The classification of a derivative instrument is reassessed at each reporting date. If the classification changes as a result of events during a reporting period, the instrument is reclassified as of the date of the event that caused the reclassification. There is no limit on the number of times a contract may be reclassified.

Instruments classified as derivative liabilities are remeasured each reporting period (or upon reclassification) and the change in fair value is recorded on our consolidated statement of operations in other (income) expense.

BENEFICIAL CONVERSION FEATURE OF CONVERTIBLE NOTES PAYABLE

The convertible feature of certain notes payable provides for a rate of conversion that is below market value. Such feature is normally characterized as a "Beneficial Conversion Feature" ("BCF"). We measure the estimated fair value of the BCF in circumstances in which the conversion feature is not required to be separated from the host instrument and accounted for separately, and record that value in the consolidated financial statements as a discount from the face amount of the notes. Such discounts are amortized to interest expense over the term of the notes.

AETHLON MEDICAL, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

MARCH 31, 2014 AND 2013

REGISTRATION PAYMENT ARRANGEMENTS

We account for contingent obligations to make future payments or otherwise transfer consideration under a registration payment arrangement separately from any related financing transaction agreements, and any such contingent obligations are recognized only when it is determined that it is probable that the Company will become obligated for future payments and the amount, or range of amounts, of such future payments can be reasonably estimated.

RESEARCH AND DEVELOPMENT EXPENSES

Our research and development costs are expensed as incurred. We incurred approximately \$1,509,000 and \$1,440,000 of research and development expenses for the years ended March 31, 2014 and 2013, respectively, which are included in various operating expenses in the accompanying consolidated statements of operations.

OFF-BALANCE SHEET ARRANGEMENTS

We have not entered into any off-balance sheet arrangements that have or are reasonably likely to have a current or future material effect on our consolidated financial statements.

SIGNIFICANT RECENT ACCOUNTING PRONOUNCEMENTS

Management is evaluating significant recent accounting pronouncements that are not yet effective for the Company, including the new accounting standard on revenue recognition, ASU 2014-09 (Topic 606), and has not yet concluded whether any such pronouncements will have a significant effect on the Company's future consolidated financial statements.

2. PROPERTY AND EQUIPMENT

Property and equipment, net, consist of the following:

	March 31, 2014	March 31, 2013
Furniture and office equipment, at cost	\$385,088	\$289,031
Accumulated depreciation	(300,809)	(288,886)
	\$84,279	\$145

Depreciation expense for the years ended March 31, 2014 and 2013 approximated \$12,000 and \$1,000, respectively.

3. PATENTS

Patents consist of the following:

	March 31, 2014	March 31, 2013
Patents	\$157,442	\$157,442
Patents pending and trademarks	54,203	54,203
Accumulated amortization	(99,156)	(89,992)
	\$112,489	\$121,653

Amortization expense for patents for the years ended March 31, 2014 and 2013 approximated \$9,000. Future amortization expense on patents is estimated to be approximately \$9,000 per year based on the estimated life of the patents. The weighted average remaining life of our patents is approximately 6.5 years.

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AETHLON MEDICAL, INC. AND SUBSIDIARY**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****MARCH 31, 2014 AND 2013****4. NOTES PAYABLE**

Notes payable consist of the following:

	March 31, 2014		March 31, 2013	
	Principal Balance	Accrued Interest	Principal Balance	Accrued Interest
12% Notes payable, past due	\$185,000	\$353,813	\$185,000	\$326,062
10% Note payable, past due	5,000	6,375	5,000	5,875
Directors' Note(s)	200,000	14,516	–	–
Tonaquint Note	–	–	131,381	1,629
Total	\$390,000	\$374,704	\$321,381	\$333,566

During the fiscal year ended March 31, 2014, we recorded interest expense of \$59,901 related to the contractual interest rates of our notes payable.

12% NOTES

From August 1999 through May 2005, we entered into various borrowing arrangements for the issuance of notes payable from private placement offerings (the "12% Notes"). On April 21, 2010, a holder of \$100,000 of the 12% Notes converted his principal balance and \$71,758 of accrued interest into 687,033 shares of common stock at an agreed conversion price of \$0.25 per share. At March 31, 2014, the 12% Notes were past due, in default, and bearing interest at the default rate of 15%.

10% NOTES

At March 31, 2014, one 10% Note in the amount of \$5,000, which is past due and in default, remained outstanding and it bears interest at the default rate of 15%.

Management's plans to satisfy the remaining outstanding balance on these 12% and 10% Notes include converting the notes to common stock at market value or repayment with available funds.

TONAQUINT NOTE

On June 28, 2011, in conjunction with our satisfying all balances owed under a convertible note, we entered into a Termination Agreement with Tonaquint, Inc. under which both parties agreed that in consideration of the termination of a warrant, the waiving of all fees, penalties, the creation of the selling program and other factors, we agreed to issue an unsecured non-convertible promissory note (the "New Note") in the principal amount of \$360,186, which provides for annual interest at a rate of 6%, payable monthly in either cash or our stock, at our option. The New Note originally had a maturity date of April 30, 2012. We subsequently extended the note initially to July 31, 2012 and then to July 31, 2013 and subsequently to August 31, 2013. We also recorded into principal \$12,500 of the lender's legal fees related to documentation of the extension agreement.

During the fiscal year ended March 31, 2014, we issued 1,540,426 shares of common stock to convert \$136,060 of principal and accrued interest (see Note 6). As a result of those conversions, the Tonaquint Note was paid off in full during the September 2013 quarter. We recorded a loss on conversion of \$40,256 on those conversions during the fiscal year ended March 31, 2014.

The following table shows the conversions into principal of the Tonaquint Note by fiscal year:

Initial principal balance	\$360,186
Lender's legal fees	12,500
Conversions during the fiscal year ended March 31, 2013	(241,305)
Conversions during the fiscal year ended March 31, 2014	(131,381)
Balance as of March 31, 2014	\$-

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AETHLON MEDICAL, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

MARCH 31, 2014 AND 2013

DIRECTORS' NOTES

In July 2013, we borrowed \$400,000 from two of our directors under two 90 day notes for \$200,000 each bearing 10% interest (the "Notes"). At the discretion of the holders, if not paid off by October 9, 2013, the noteholders were entitled to (i) convert their principal and accrued interest into shares of common stock at \$0.088 per share (the "Conversion Price") and (ii) receive warrants to purchase common stock equal to 50% of the principal converted under the Notes, with an exercise price of \$0.132 per share. Additionally, there was a provision for a penalty interest rate of 12%.

That potential conversion price and warrant exercise price were based on the same pricing mechanism that we have used in prior equity unit financings since March 2012 (see Note 6) which are based on 80% of the then current market price of our common stock and with the warrant exercise price based on 120% of the same then current market price. We initially reserved 6,931,818 shares of common stock to support the conversion of the Notes and accrued interest in full as well as the exercise of the warrants in full (should such conversion and/or issuance occur).

During the fiscal year ended March 31, 2014, the principal of \$200,000 and accrued interest of \$9,367 were paid on one of the notes, which extinguished all potential common stock and warrant issuance provisions related to that Note.

The holder of the second Note agreed to extend the expiration date of his Note to July 31, 2014.

5. CONVERTIBLE NOTES PAYABLE

Convertible Notes Payable consisted of the following at March 31, 2014:

	Principal	Unamortized Discount	Net Amount	Accrued Interest
Convertible Notes Payable – Current Portion:				

Explanation of Responses:

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Amended and Restated Series A 12% Convertible Notes, past due	\$885,000	\$	–	\$885,000	\$575,250
2008 10% Convertible Notes, past due	25,000	–	–	25,000	19,167
October & November 2009 10% Convertible Notes	50,000	–	–	50,000	26,097
April 2010 10% Convertible Note	75,000	–	–	75,000	31,438
July and August 2011 10% Convertible Notes, past due	257,655	–	–	257,655	90,256
Law Firm Note	75,000	–	–	75,000	7,604
Total – Convertible Notes Payable – Current Portion	1,367,655	–	–	1,367,655	749,812
Convertible Notes Payable – Non-Current Portion:					
September 2010 12% Convertible Notes	317,072	–	–	317,072	35,034
April 2011 12% Convertible Notes	448,448	–	–	448,448	12,117
September 2011 12% Convertible Notes	10,931	–	–	10,931	--
Total – Convertible Notes Payable – Non-Current Portion	776,451	–	–	776,451	47,151
Total Convertible Notes Payable	\$2,144,106	\$	–	\$2,144,106	\$796,963

There were no discounts remaining on any of our Convertible Notes Payable as of March 31, 2014.

During the fiscal year ended March 31, 2014, we recorded interest expense of \$354,949 related to the contractual interest rates of our convertible notes and interest expense of \$4,284 related to the amortization of debt discounts on the convertible notes for a total of \$359,233.

AETHLON MEDICAL, INC. AND SUBSIDIARY**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****MARCH 31, 2014 AND 2013**

Convertible Notes Payable consisted of the following at March 31, 2013:

	Principal	Unamortized Discount	Net Amount	Accrued Interest
Amended and Restated Series A 12% Convertible Notes, past due	\$885,000	\$ –	\$885,000	\$398,250
2008 10% Convertible Notes, past due	25,000	–	25,000	15,417
December 2006 10% Convertible Notes, past due	17,000	–	17,000	15,888
October & November 2009 10% Convertible Notes	50,000	(389)	49,611	20,000
April 2010 10% Convertible Note	75,000	(3,895)	71,105	23,938
September 2010 10% Convertible Notes, past due	308,100	–	308,100	52,393
April 2011 10% Convertible Notes, past due	400,400	–	400,400	100,100
July and August 2011 10% Convertible Notes, \$257,656 past due	357,655	–	357,655	68,704
September 2011 Convertible Notes, past due	178,760	–	178,760	–
Law Firm Note	75,000	–	75,000	3,854
Total – Convertible Notes Payable	\$2,371,915	\$ (4,284)	\$2,367,631	\$698,544

During the fiscal year ended March 31, 2013, we recorded interest expense of \$459,199 related to the contractual interest rates of our convertible notes and interest expense of \$467,158 related to the amortization of debt discounts on the convertible notes for a total of \$926,357.

AMENDED AND RESTATED SERIES A 12% CONVERTIBLE NOTES

In June 2010, we entered into Amended and Restated Series A 12% Convertible Promissory Notes (the "Amended and Restated Notes") with the holders of certain promissory notes previously issued by the Company, extending the due date to December 31, 2010 on the aggregate principal balance of \$900,000. During the fiscal year ended March 31, 2013, the holders of \$15,000 of the Notes converted their principal and related accrued interest into common stock. The balance remaining at March 31, 2014 and 2013 was \$885,000 and is past due as of March 31, 2014. Such notes bear a default annual interest rate of 20%.

Subsequent to year end on June 24, 2014, we entered into an agreement with the Ellen R. Weiner Family Revocable Trust (the "Trust"), a holder of a Series A 12% Convertible Note (the "Note"), whereby the Trust converted a past due combined principal and interest balance of \$1,003,200 (principal of \$660,000 and interest of \$343,200) into restricted common stock.

Additionally, the Trust agreed to waive anti-dilution price protection underlying warrants previously issued to the Trust. Under its agreement, the Trust converted the entire \$1,003,200 past due principal and interest balance on the Note

In exchange for the Trust's conversion in full of the Note and accrued interest and for the waivers of anti-dilution price protection in previously issued warrants, we (1) issued five-year warrants to acquire up to 6,809,524 shares of our common stock at an exercise price of \$.042 per share and up to 397,222 shares of our common stock at an exercise price of \$.108 per share (collectively, the "Conversion Securities"); (2) issued 75,000 restricted shares of common stock as a service fee; (3) changed the exercise price of all of the previously issued warrants to the Trust to \$.042 per share; and (4) extended the expiration date of all of the previously issued warrants to the Trust to July 1, 2018.

We continue to hold discussions with the holder of the remaining note in this grouping regarding either an extension to the note or a conversion of the note but there can be no assurance that we will be able to do so on terms that we deem acceptable or at all. We are recording interest at the default rate of 20% on the remaining note.

DECEMBER 2006 10% CONVERTIBLE NOTES

In January 2014, we paid off the remaining balance of the December 2006 10% Convertible Notes and the related accrued interest balance with a cash payment of \$35,055. Such payment represented the sum of the \$17,000 in principal balance and \$18,055 in accrued interest.

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2008 10% CONVERTIBLE NOTES

One 2008 10% Convertible Note in the amount of \$25,000 which matured in January 2010 remained outstanding and past due at March 31, 2014. Such note is convertible into our common stock at \$0.50 per share. We are recording interest at the default rate of 15%.

OCTOBER & NOVEMBER 2009 10% CONVERTIBLE NOTES

In October and November 2009, we raised \$430,000 from the sale to accredited investors of 10% convertible notes ("October & November 2009 10% Convertible Notes"). The October & November 2009 10% Convertible Notes matured at various dates between April 2011 and May 2011 and are convertible into our common stock at a fixed conversion price of \$0.25 per share. The investors also received matching three year warrants to purchase unregistered shares of our common stock at an exercise price of \$0.25 per share. We measured the fair value of the warrants and the beneficial conversion feature of the notes and recorded a 100% discount against the principal of the notes. Such discount was fully amortized at March 31, 2014.

In July 2012, we issued 461,409 shares of common stock and 230,705 warrants to purchase common stock to the holder of a \$25,000 note in this grouping in exchange for the conversion of such note and related accrued interest of \$8,000 (for a total of \$33,000). The warrants expired in 2012 and are exercisable at \$0.107 per share (see Note 6). We recorded a loss on conversion of \$45,796.

The following table shows the conversions into principal of the October and November 2009 Convertible Notes by fiscal year:

Activity in October & November 2009 10% Convertible Notes	
Initial principal balance	\$450,250
Conversions during the fiscal year ended March 31, 2010	(70,000)
Conversions during the fiscal year ended March 31, 2011	(175,000)
Conversions during the fiscal year ended March 31, 2012	(130,250)
Conversions during the fiscal year ended March 31, 2013	(25,000)
Conversions during the fiscal year ended March 31, 2014	--
Balance as of March 31, 2014	\$50,000

On March 31, 2012, we agreed to extend the expiration date and to change the exercise price of certain warrants of one of the note holders by two years in exchange for the extension of \$50,000 of the October & November 2009 10%

Convertible Notes and the \$75,000 April 2010 10% Convertible Note (see below) by that same two year period. We recorded a charge of \$77,265 relating to this modification.

In September 2013, we agreed to extend the expiration date of certain warrants of one of the note holders by two years in exchange for the extension of \$50,000 of the October & November 2009 10% Convertible Notes and the \$75,000 April 2010 10% Convertible Note (see below) by that same two year period. Management assessed the change in the value of the notes and related warrants before and after that extension and determined that the change in value related to the change in terms was not significant.

APRIL 2010 10% CONVERTIBLE NOTE

In April 2010, we raised \$75,000 from the sale to an accredited investor of a 10% convertible note. The convertible note was originally scheduled to mature in October 2011 and is convertible into our common stock at a fixed conversion price of \$0.25 per share prior to maturity. The investor also received three year warrants to purchase 300,000 unregistered shares of our common stock at a price of \$0.25 per share.

We measured the fair value of the warrants and the beneficial conversion feature of the notes and recorded a 100% discount against the principal of the notes. We amortized this discount using the effective interest method over the term of the note. As of March 31, 2014, there have not been any conversions of the April 2010 10% Convertible Note.

On March 31, 2012, we agreed to extend the expiration date and to change the exercise price of certain warrants of the note holder by two years in exchange for his extension of \$50,000 of the October & November 2009 10% Convertible Notes and the \$75,000 April 2010 10% Convertible Note by that same two year period.

In September 2013, we agreed to extend the expiration date of certain warrants of one of the note holders by two years in exchange for the extension of \$50,000 of the October & November 2009 10% Convertible Notes and the \$75,000 April 2010 10% Convertible Note (see below) by that same two year period. Management assessed the change in the value of the notes and related warrants before and after that extension and determined that the change in value related to the change in terms was not significant.

SEPTEMBER 2010 10% CONVERTIBLE NOTES

On September 3, 2010, we entered into a Subscription Agreement with three accredited investors (the “Purchasers”) providing for the issuance and sale of convertible promissory notes and corresponding warrants in the aggregate principal amount of \$1,430,000. The initial closing under the Subscription Agreement resulted in the issuance and sale of (i) convertible promissory notes in the aggregate principal amount of \$743,600, (ii) five-year warrants to purchase an aggregate of 3,718,000 shares of our common stock at an exercise price of \$0.31125 per share, and (iii) five-year warrants to purchase an aggregate of 3,718,000 shares of our common stock at an exercise price of \$0.43575 per share. The convertible promissory notes bear interest compounded monthly at the annual rate of ten percent (10%) and mature on April 1, 2016 (see below). The aggregate gross cash proceeds were \$650,000, the balance of the principal amount representing a due diligence fee and an original issuance discount. The convertible promissory notes are convertible at the option of the holders into shares of our common stock at a price per share equal to eighty percent (80%) of the average of the three lowest closing bid prices of the common stock as reported by Bloomberg L.P. for the principal market on which the common stock trades or is quoted for the ten (10) trading days preceding the proposed conversion date. Subject to adjustment as described in the notes, the conversion price may not be more than \$0.30 nor less than \$0.20. There are no registration requirements with respect to the shares of common stock underlying the notes or the warrants.

On March 31, 2014, we entered into separate Amendments to Convertible Notes and Warrants (collectively, the “Amendments”) with three accredited investors (collectively, the “Investors”) who own certain convertible promissory notes (collectively, the “Notes”) and warrants (collectively, the “Warrants”) previously issued by us on various dates between December 5, 2007 and September 23, 2011, including the September 2010 Convertible Notes.

Prior to the Amendments, the Notes were past maturity and were in default, resulting in the accrual of interest at the applicable default interest rate. The Amendments extended the maturity date of each of the Notes to April 1, 2016, which permits us to classify them as long-term liabilities. As a result of the Amendments, the Notes are no longer in default and the non-default interest rate for all of the Notes was set at 12% per annum, which represents a reduction from the default interest rates of fifteen percent at which interest had been accruing. By entering into the Amendments, we also agreed to increase the currently outstanding principal amount of the Notes by 12% from a total of \$693,260 to a total of \$776,451.

During the period from October 2011 to February 2014, the Investors had converted, at conversion prices between \$.0546 and \$.07 per share, portions of principal and interest outstanding under the Notes and certain other convertible promissory notes previously issued to them by us. Certain antidilution provisions applicable to such notes should have resulted in such conversions being effected at a conversion price of \$.042 per share. Accordingly, pursuant to the Amendments, we issued to the investors an aggregate of 4,507,105 shares of the Company’s Common Stock, which represents the additional shares of Common Stock that would have been issued to the Investors had such conversions been effected at \$.042 per share.

The Amendments also provide that if all of our currently outstanding promissory notes and warrants that contain antidilution adjustment provisions (other than the Investors' Notes and Warrants) are amended to remove, or the holders thereof waive, such provisions, then any similar antidilution provisions in the Investors' Notes and Warrants will automatically be deemed removed. In addition, for so long as the Investors' Notes and Warrants are outstanding, we will not be permitted to issue any common stock or common stock equivalents (or modify, with equivalent effect, any outstanding common stock or common stock equivalents) at a lower price than the then-current conversion price of the Notes and exercise price of the Warrants (with certain issuances to be excepted from this general provision). If our other note and warrant holders agree to waive the antidilution provisions of their securities on the same basis as agreed to by the Investors, then we will no longer be required to report a derivative liability in its financial statements with the accompanying quarterly adjustments to its financial statements and will transfer the amount shown as a derivative liability to equity.

The Amendments also set the conversion price of the Notes, as well as the exercise price at which shares of our common stock can be purchased under the Warrants, at \$.042 per share. By virtue of the Amendments, the expiration dates of the Warrants also were extended from dates between September 3, 2015 and September 23, 2016 to January 1, 2017.

The following table shows the activity in the September 2010 10% Convertible Notes by fiscal year:

Activity in the September 2010 10% Convertible Notes	
Initial principal balance	\$743,600
Conversions during the fiscal year ended March 31, 2012	(405,500)
Conversions during the fiscal year ended March 31, 2013	(30,000)
Conversions during the fiscal year ended March 31, 2014	(25,000)
Increase in principal balance due to 12% extension fee	33,972
Balance as of March 31, 2014	\$317,072

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APRIL 2011 10% CONVERTIBLE NOTES

In April 2011, we entered into a Subscription Agreement with two accredited investors (the “Purchasers”) providing for the issuance and sale of convertible promissory notes and corresponding warrants in the aggregate principal amount of \$385,000. The closing under the Subscription Agreement resulted in the issuance and sale by us of (i) convertible promissory notes in the aggregate principal amount of \$385,000, (ii) five-year warrants to purchase an aggregate of 4,004,000 shares of our common stock at an exercise price of \$0.125 per share, and (iii) five-year warrants to purchase an aggregate of 4,004,000 shares of our common stock at an exercise price of \$0.175 per share. The convertible promissory notes bear interest compounded monthly at the annual rate of 10% and mature on April 1, 2016 (see below). The aggregate gross cash proceeds to us were \$350,000, the balance of the principal amount representing a due diligence fee and an original issuance discount. The convertible promissory notes are convertible at the option of the holders into shares of our common stock at a price per share equal to eighty percent (80%) of the average of the three lowest closing bid prices of the common stock as reported by Bloomberg L.P. for the principal market on which the common stock trades or is quoted for the ten (10) trading days preceding the proposed conversion date. Subject to adjustment as described in the notes, the conversion price may not be more than \$0.20 nor less than \$0.10. There are no registration requirements with respect to the shares of common stock underlying the notes or the warrants.

In addition, we issued (i) five-year warrants to purchase an aggregate of 812,500 shares of our common stock at an exercise price of \$0.125 per share, and (ii) five-year warrants to purchase an aggregate of 812,500 shares of our common stock at an exercise price of \$0.175 per share to the Purchasers. These warrants were issued as an antidilution adjustment under certain common stock purchase warrants held by the Purchasers that were acquired from us in September 2010.

On March 31, 2014, we entered into separate Amendments to Convertible Notes and Warrants (collectively, the “Amendments”) with three accredited investors (collectively, the “Investors”) who own certain convertible promissory notes (collectively, the “Notes”) and warrants (collectively, the “Warrants”) previously issued by us on various dates between December 5, 2007 and September 23, 2011, including the April 2011 Convertible Notes.

Prior to the Amendments, the Notes were past maturity and were in default, resulting in the accrual of interest at the applicable default interest rate. The Amendments extended the maturity date of each of the Notes to April 1, 2016, which permits us to classify them as long-term liabilities. As a result of the Amendments, the Notes are no longer in default and the non-default interest rate for all of the Notes was set at 12% per annum, which represents a reduction from the default interest rates of 15% at which interest had been accruing. By entering into the Amendments, we also agreed to increase the currently outstanding principal amount of the Notes by 12% from a total of \$693,260 to a total of \$776,451.

During the period from October 2011 to February 2014, the Investors had converted, at conversion prices between \$.0546 and \$.07 per share, portions of principal and interest outstanding under the Notes and certain other convertible promissory notes previously issued to them by us. Certain antidilution provisions applicable to such notes should have resulted in such conversions being effected at a conversion price of \$.042 per share. Accordingly, pursuant to the Amendments, we issued to the investors an aggregate of 4,507,105 shares of the Company's Common Stock, which represents the additional shares of Common Stock that would have been issued to the Investors had such conversions been effected at \$.042 per share.

The Amendments also provide that if all of our currently outstanding promissory notes and warrants that contain antidilution adjustment provisions (other than the Investors' Notes and Warrants) are amended to remove, or the holders thereof waive, such provisions, then any similar antidilution provisions in the Investors' Notes and Warrants will automatically be deemed removed. In addition, for so long as the Investors' Notes and Warrants are outstanding, we will not be permitted to issue any common stock or common stock equivalents (or modify, with equivalent effect, any outstanding common stock or common stock equivalents) at a lower price than the then-current conversion price of the Notes and exercise price of the Warrants (with certain issuances to be excepted from this general provision).

The Amendments also set the conversion price of the Notes, as well as the exercise price at which shares of our common stock can be purchased under the Warrants, at \$.042 per share. By virtue of the Amendments, the expiration dates of the Warrants also were extended from dates between September 3, 2015 and September 23, 2016 to January 1, 2017.

As of March 31, 2014, there have not been any conversions of the April 2011 10% Convertible Notes and the 12% extension fee noted above increased the principal balance by \$48,048 to a principal balance of \$448,448.

JULY & AUGUST 2011 10% CONVERTIBLE NOTES

During the three months ended September 30, 2011, we raised \$357,656 in 10% convertible notes. Those notes had a fixed conversion price of \$0.09 per share and carried an interest rate of 10%. The convertible notes matured in July and August 2012. We also issued those investors five year warrants to purchase 3,973,957 shares of common stock at \$0.125 per share.

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We measured the fair value of the warrants and the beneficial conversion feature of the notes and recorded a \$257,926 discount against the principal of the notes. We amortized this discount using the effective interest method over the term of the note.

Effective March 31, 2014, the holders of the three notes totaling \$100,000 converted all of their principal and accrued interest into 1,438,700 shares of our common stock at the contractual conversion price of \$0.09 per share.

At March 31, 2014, the remaining outstanding principal balance was \$257,655, all of which was in default. We are recording interest at the default interest rate of 15%.

SEPTEMBER 2011 CONVERTIBLE NOTES

In September 2011, we issued \$253,760 of convertible notes, convertible at \$0.07 per share. Such notes originally matured in September 2012.

On March 31, 2014, we entered into separate Amendments to Convertible Notes and Warrants (collectively, the "Amendments") with three accredited investors (collectively, the "Investors") who own certain convertible promissory notes (collectively, the "Notes") and warrants (collectively, the "Warrants") previously issued by us on various dates between December 5, 2007 and September 23, 2011, including the September 2011 Convertible Notes.

Prior to the Amendments, the Notes were past maturity and were in default, resulting in the accrual of interest at the applicable default interest rate. The Amendments extended the maturity date of each of the Notes to April 1, 2016, which permits us to classify them as long-term liabilities. As a result of the Amendments, the Notes are no longer in default and the non-default interest rate for all of the Notes was set at 12% per annum, which represents a reduction from the default interest rates of 15% at which interest had been accruing. By entering into the Amendments, we also agreed to increase the currently outstanding principal amount of the Notes by 12%, which in the case of the September 2011 Notes, they increased from \$9,760 to \$10,931

During the period from October 2011 to February 2014, the Investors had converted, at conversion prices between \$.0546 and \$.07 per share, portions of principal and interest outstanding under the Notes and certain other convertible promissory notes previously issued to them by us. Certain antidilution provisions applicable to such notes should have resulted in such conversions being effected at a conversion price of \$.042 per share. Accordingly, pursuant to the Amendments, we issued to the investors an aggregate of 4,507,105 shares of the Company's Common Stock, which represents the additional shares of Common Stock that would have been issued to the Investors had such conversions

been effected at \$.042 per share.

The Amendments also provide that if all of our currently outstanding promissory notes and warrants that contain antidilution adjustment provisions (other than the Investors' Notes and Warrants) are amended to remove, or the holders thereof waive, such provisions, then any similar antidilution provisions in the Investors' Notes and Warrants will automatically be deemed removed. In addition, for so long as the Investors' Notes and Warrants are outstanding, we will not be permitted to issue any common stock or common stock equivalents (or modify, with equivalent effect, any outstanding common stock or common stock equivalents) at a lower price than the then-current conversion price of the Notes and exercise price of the Warrants (with certain issuances to be excepted from this general provision). If our other note and warrant holders agree to waive the antidilution provisions of their securities on the same basis as agreed to by the Investors, then we will no longer be required to report a derivative liability in its financial statements with the accompanying quarterly adjustments to its financial statements and will transfer the amount shown as a derivative liability to equity.

The Amendments also set the conversion price of the Notes, as well as the exercise price at which shares of our common stock can be purchased under the Warrants, at \$.042 per share. By virtue of the Amendments, the expiration dates of the Warrants also were extended to January 1, 2017.

The following table shows the conversions into principal of the September 2011 Convertible Notes by fiscal year:

Activity in the September 2011 Convertible Notes	
Initial principal balance	\$253,760
Conversions during the fiscal year ended March 31, 2012	(15,000)
Conversions during the fiscal year ended March 31, 2013	(60,000)
Conversions during the fiscal year ended March 31, 2014	(169,000)
Increase in principal balance due to extension fee	1,171
Balance as of March 31, 2014	\$10,931

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LAW FIRM NOTE NUMBER 1

On March 22, 2012, we entered into a Promissory Note with our corporate law firm for the amount of \$75,000, which represented the majority of the amount we owed to that firm at that time. The Promissory Note originally had a maturity date of December 31, 2012 and bears interest at 5% per annum. The note is convertible at the option of the holder into shares of our common stock at a 10% discount to the market price of the common stock on the date prior to conversion with a floor price on such conversions of \$0.08 per share. The holder subsequently agreed to extend the Maturity Date of the Note first to October 1, 2013, then to September 30, 2013, and now the expiration date of this note is again extended to October 1, 2014. As of March 31, 2014, there have not been any conversions of the Law Firm Note.

LAW FIRM NOTE NUMBER 2

On June 4, 2013, we entered into a Promissory Note with our corporate law firm for the amount of \$47,000, which represented approximately 50% of the amount we owed to that firm for services in 2012. The Promissory Note had a maturity date of October 1, 2014 and bore interest at 5% per annum. The note was convertible at the option of the holder into shares of our common stock at a 10% discount to the market price of the common stock on the date prior to conversion with a floor price on such conversions of \$0.07 per share.

Effective March 31, 2014, our law firm converted this note and all related accrued interest into 302,043 shares of our common stock at a conversion price of \$0.16 per share.

6. EQUITY TRANSACTIONS

COMMON STOCK AND WARRANTS

Aethlon Medical, Inc. Equity Transactions in the Fiscal Year Ended March 31, 2014

Common Stock Issuances in the Fiscal Year Ended March 31, 2014:

In June 2013, we completed a unit subscription agreement with three accredited investors pursuant to which we issued 1,580,248 shares of our common stock and 790,124 warrants to purchase our common stock for net cash proceeds of \$128,000. Such warrants have an exercise price of \$0.121 per share.

In June 2013, we issued to our CEO the remaining 3,400,000 shares under his restricted share grant, all of which were vested.

During the three months ended June 30, 2013, we issued 3,675,278 shares of restricted common stock to the holders of three notes issued by the Company in exchange for the partial conversion of principal and interest in an aggregate amount of \$246,500 at an average conversion price of \$0.07 per share.

During the three months ended June 30, 2013, we issued 222,734 shares of common stock pursuant to our S-8 registration statement covering our Amended 2010 Stock Plan at an average price of \$0.10 per share in payment for legal services valued at \$21,750 based on the value of the services provided.

In August 2013, we completed a unit subscription agreement with four accredited investors (the "Purchasers") pursuant to which we issued 900,901 shares of our common stock and 450,451 warrants to purchase our common stock in exchange for net cash proceeds of \$100,000. Such warrants have an exercise price of \$0.167 per share.

During the three months ended September 30, 2013, we issued 933,522 shares of common stock pursuant to our S-8 registration statement covering our Amended 2010 Stock Plan at an average price of \$0.14 per share in payment for legal and scientific consulting services valued at \$127,593 based on the value of the services provided.

During the three months ended September 30, 2013, we issued 1,168,343 shares of restricted common stock at an average price of \$0.10 per share in payment for investor relations and public relations services valued at \$115,000 based on the value of the services provided.

During the three months ended September 30 2013, we issued 2,795,367 shares of restricted common stock to the holders of four notes issued by the Company in exchange for the partial or full conversion of principal and interest in an aggregate amount of \$173,960 at an average conversion price of \$0.06 per share.

During the three months ended December 31, 2013, we entered into a unit purchase agreement and subscription agreements with 32 accredited investors pursuant to which we issued 14,367,200 shares of our common stock and warrants to purchase our common stock for gross cash proceeds of \$1,795,900. Such warrants have an exercise price of \$0.22 per share. A FINRA registered broker-dealer was engaged as placement agent in connection with the above

Unit Purchase Agreement. We paid the placement agent an aggregate cash fee in the amount of \$270,508 and will issue the placement agent or its designees warrants to purchase an aggregate of 2,155,080 shares of our common stock. We also paid \$78,360 in other costs and fees, including legal fees, blue sky fees and escrow costs. The net proceeds that we received totaled \$1,447,032.

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AETHLON MEDICAL, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

MARCH 31, 2014 AND 2013

During the three months ended December 31 2013, we issued 1,465,200 shares of restricted common stock to the holders of two notes issued by us in exchange for the partial or full conversion of accrued interest in an aggregate amount of \$80,000 at an average conversion price of \$0.05 per share.

During the three months ended March 31 2014, we issued 2,638,179 shares of restricted common stock to the holders of five notes issued by us in exchange for the partial or full conversion of accrued interest in an aggregate amount of \$226,316 at an average conversion price of \$0.09 per share.

During the three months ended March 31, 2014, we issued 346,770 shares of common stock pursuant to our S-8 registration statement covering our Amended 2010 Stock Plan at an average price of \$0.19 per share in payment for legal services valued at \$65,250 based on the value of the services provided.

During the three months ended March 31, 2014, we issued 399,781 shares of restricted common stock at an average price of \$0.16 per share in payment for investor relations and public relations services valued at \$62,500 based on the value of the services provided.

On March 31, 2014, we entered into extension agreements with three noteholders (see Note 5). In conjunction with the extension agreements, we agreed to issue to the noteholders an aggregate 4,507,105 shares of restricted common stock as a result of the noteholders invoking the antidilution protection on their notes.

In March 2014, a former director exercised 182,927 in vested stock options through the contribution of \$2,000 in cash and \$13,000 in accrued expenses owed to him based on the exercise price of \$0.082 per share.

During the fiscal year ended March 31, 2014, we issued 12,716,225 shares of restricted common stock in connection with cashless warrant exercises discussed elsewhere in this footnote.

Exosome Sciences, Inc. Equity Transactions in the Fiscal Year Ended March 31, 2014

On November 21, 2013, ESI, prior to the transaction described herein, a wholly owned diagnostic subsidiary of ours, entered into a stock purchase agreement with twelve accredited investors pursuant to which such investors purchased an aggregate of 220,000 shares of ESI's common stock at a purchase price of \$5.00 per share, for an aggregate purchase price of \$1,100,000 in cash.

On December 13, 2013, ESI entered into a second stock purchase agreement with three accredited investors, pursuant to which such investors purchased an aggregate of 80,000 shares of ESI's common stock at a purchase price of \$5.00 per share, for an aggregate purchase price of \$400,000 in cash.

The aggregate gross proceeds received by ESI under these two transactions above were \$1,500,000. As a result of these transactions the Company's percentage ownership of the outstanding common stock of ESI was reduced from 100% to 80%.

One of the investors was Dr. Chetan Shah, a director of the Company. Dr. Shah purchased 70,000 ESI shares for an aggregate purchase price of \$350,000.

Common Stock Issuances in the Fiscal Year Ended March 31, 2013:

During the fiscal year ended March 31, 2013, we issued 22,829,754 shares of restricted common stock to holders of notes issued by the Company in exchange for the partial or full conversion of principal and interest of several notes payable in an aggregate amount of \$1,707,052 at an average conversion price of \$0.07 per share based upon the conversion formulae in the respective notes.

During the fiscal year ended March 31, 2013, we issued 1,932,808 restricted shares of common stock to service providers for investor relations, corporate communications and business development services valued at \$170,849 based upon the fair value of the shares issued. The average issuance price on the restricted share issuances was approximately \$0.09 per share.

During the fiscal year ended March 31, 2013, we issued 963,373 shares of common stock pursuant to our S-8 registration statement covering our Amended 2010 Stock Plan at an average price of \$0.09 per share in payment for scientific consulting services valued at \$88,186 based on the value of the services provided.

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AETHLON MEDICAL, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

MARCH 31, 2014 AND 2013

On April 5, 2012, we completed a unit subscription agreement with one accredited investor (the “Purchaser”) pursuant to which we issued 2,500,000 shares of our common stock and 1,250,000 warrants to purchase our common stock for net cash proceeds of \$200,000. Such warrants have an exercise price of \$0.125 per share.

On June 19, 2012, we completed a unit subscription agreement whereby we issued 8,222,222 shares of our common stock and 4,111,111 warrants to purchase our common stock at an exercise price of \$0.108 per share in exchange for net cash proceeds of \$592,000.

On June 26, 2012, we completed a unit subscription agreement whereby we issued 139,821 shares of our common stock and 69,911 warrants to purchase our common stock at an exercise price of \$0.107 per share in exchange for net cash proceeds of \$10,000.

In July 2012, we issued 461,409 shares of common stock to the holder of a \$25,000 October & November 2009 10% Convertible Note (See Note 5) in exchange for the value of the principal and related accrued interest of \$8,000 under the same terms that we used to sell units consisting of one share of common stock and one-half of a stock purchase warrant on June 29, 2012 (See Note 6). As part of that structure, the noteholder also received seven year warrants to purchase 230,705 shares of our common stock at an exercise price of \$0.107 per share.

On August 29, 2012, we completed a unit subscription agreement with seven accredited investors pursuant to which we issued 3,387,500 shares of our common stock and 1,693,750 warrants to purchase our common stock in exchange for net cash proceeds of \$271,000. Such warrants have an exercise price of \$0.12 per share.

Between October 2012 and December 2012, we completed several unit subscription agreements with several accredited investors pursuant to which we issued 7,878,580 shares of our common stock and 3,939,292 warrants to purchase our common stock for net cash proceeds of \$498,000. Such warrants have an exercise price based upon 120% of the average of the closing prices of our common stock for the five-day period immediately preceding the respective investment transaction date.

In January 2013, we issued 246,429 shares of restricted common stock to the owner of a patent as a patent license payment valued at \$17,250.

Between January 2013 and March 2013, we completed several unit subscription agreements with several accredited investors pursuant to which we issued 7,596,423 shares of our common stock and 3,798,219 warrants to purchase our common stock for net cash proceeds of \$538,834. Such warrants have an exercise price based upon 120% of the average of the closing prices of our common stock for the five-day period immediately preceding the respective investment transaction date.

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AETHLON MEDICAL, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

MARCH 31, 2014 AND 2013

A summary of the aggregate warrant activity for the years ended March 31, 2014 and 2013 is presented below:

	Year Ended March 31,		2013	
	2014	Weighted Average Exercise Price	Warrants	Weighted Average Exercise Price
Outstanding, beginning of year	75,647,294	\$ 0.11	59,807,849	\$ 0.14
Granted	14,530,519	\$ 0.18	16,710,445	\$ 0.11
Exercised	(12,716,225)	\$ 0.08	—	\$ —
Cancelled/Forfeited	(6,752,113)	\$ 0.11	(871,000)	\$ 0.25
Outstanding, end of year	70,709,475	\$ 0.10	75,647,294	\$ 0.11
Exercisable, end of year	70,709,475	\$ 0.10	75,647,294	\$ 0.11
Weighted average estimated fair value of warrants granted		\$ 0.09		\$ 0.07

The following outlines the significant weighted average assumptions used to estimate the fair value of warrants granted utilizing the Binomial Lattice option pricing model:

	Year Ended March 31,	
	2014	2013
Risk free interest rate	1.3%-2.04%	0.86%-1.56%
Average expected life	5 to 7 years	5 to 7 years
Expected volatility	91.2% - 98.5%	90.3% - 94.3%
Expected dividends	None	None

The detail of the warrants outstanding and exercisable as of March 31, 2014 is as follows:

Range of Exercise Prices	Warrants Outstanding		Warrants Exercisable	
	Number	Weighted Average	Number	Weighted Average
	Outstanding		Outstanding	

Explanation of Responses:

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	Remaining	Exercise		Exercise	
		Price		Price	
	Life				
	(Years)				
\$0.10 or Below	37,094,795	2.42	\$ 0.05	37,094,795	\$ 0.05
\$0.11 - \$0.19	21,876,000	4.74	\$ 0.13	21,876,000	\$ 0.13
\$0.20 - \$0.25	11,738,680	5.05	\$ 0.21	11,738,680	\$ 0.21
	70,709,475			70,709,475	

STOCK OPTIONS:

2000 STOCK OPTION PLAN

Our 2000 Stock Option Plan (the "Plan"), adopted by us in August 2000, provides for the grant of incentive stock options ("ISOs") to our full-time employees (who may also be directors) and nonstatutory stock options ("NSOs") to non-employee directors, consultants, customers, vendors or providers of significant services. The exercise price of any ISO may not be less than the fair market value of our common stock on the date of grant or, in the case of an optionee who owns more than 10% of the total combined voting power of all classes of our outstanding common stock, not be less than 110% of the fair market value on the date of grant. The exercise price, in the case of any NSO, must not be less than 75% of the fair market value of our common stock on the date of grant. The amount reserved under the Plan is 500,000 options.

At March 31, 2012, all of the grants previously made under the Plan had expired and 10,000 restricted shares had been issued under the 2000 Stock Option Plan, with 490,000 available for future issuance.

2003 CONSULTANT STOCK PLAN

Our 2003 Consultant Stock Plan, as amended from time to time (the "Stock Plan"), adopted by us in August 2003, advances our interests by helping us obtain and retain the services of persons providing consulting services upon whose judgment, initiative, efforts and/or services we are substantially dependent, by offering to or providing those persons with incentives or inducements affording such persons an opportunity to become owners of our common stock. Over several years, we issued 7,500,000 shares under the Stock Plan and discontinued using the Stock Plan in October 2012.

2010 STOCK INCENTIVE PLAN

In August 2010, we adopted the 2010 Stock Incentive Plan (the "Incentive Plan"), which provides incentives to attract, retain and motivate employees and directors whose present and potential contributions are important to the success of the Company by offering them an opportunity to participate in our future performance through awards of options, the right to purchase common stock, stock bonuses and stock appreciation rights and other awards. A total of 3,500,000 common shares were initially reserved for issuance under the Incentive Plan.

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AETHLON MEDICAL, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

MARCH 31, 2014 AND 2013

In August 2010, we filed a registration statement on Form S-8 for the purpose of registering 3,500,000 common shares issuable under the Incentive Plan under the Securities Act of 1933 and in July 2012, we filed a registration statement on Form S-8 for the purpose of registering an additional 5,000,000 common shares issuable under the Incentive Plan under the Securities Act of 1933.

In May 2013, we issued to a scientific advisory board member and a scientific consultant a three year option to purchase 125,000 shares of our common stock at a price of \$0.11 per share.

At March 31, 2014, we had 2,445,626 shares available under the Incentive Plan.

2012 DIRECTORS COMPENSATION PROGRAM

In July 2012, our Board of Directors approved a new Board Compensation Program (the “New Program”), which modifies and supersedes the 2005 Directors Compensation Program (the “2005 Program”) that was previously in effect. Under the New Program, in which only non-employee Directors may participate, an eligible Director will receive a grant of \$35,000 worth of ten year options to acquire shares of our common stock, with such grant being valued at the exercise price based on the average of the closing bid prices of our common stock for the five trading days preceding the first day of the fiscal year. In addition, under the New Program, eligible Directors will receive cash compensation equal to \$500 for each committee meeting attended and \$1,000 for each formal Board meeting attended.

In the fiscal year ended March 31, 2013, our Board of Directors granted under the New Program, to our four outside directors, ten year options to acquire an aggregate of 1,667,105 shares of our common stock, all with an exercise price of \$0.076 per share.

In the fiscal year ended March 31, 2014, our Board of Directors granted under the New Program, to our five outside directors, ten year options to acquire an aggregate of 1,595,536 shares of our common stock, all with an exercise price of \$0.082 per share.

At March 31, 2014 under the 2005 Program, we had issued 1,337,825 options to outside directors and 3,965,450 options to employee-directors. Of such amounts, 514,550 outside directors' options had been forfeited, 250,000 outside directors' options had been exercised, and 3,671,550 options remained outstanding.

On June 6, 2014, our Board of Directors approved certain changes to the New Program. Under the modified New Program, a new eligible Director will receive an initial grant of \$50,000 worth of options to acquire shares of our common stock, with such grant being valued at the exercise price based on the average of the closing bid prices of our common stock for the five trading days preceding the first day of the fiscal year. These options will have a term of ten years and will vest 1/3 upon grant and 1/3 upon each of the first two anniversaries of the date of grant. In addition, at the beginning of each fiscal year, each existing Director eligible to participate in the modified New Program also will receive a grant of \$35,000 worth of options valued at the exercise price based on the average of the closing bid prices of our common stock for the five trading days preceding the first day of the fiscal year. Such options will vest on the first anniversary of the date of grant. In lieu of per meeting fees, under the modified New Program eligible Directors will receive an annual Board cash retainer fee of \$30,000. The modified New Program also provides for the following annual cash retainer fees: Audit Committee Chair - \$5,000, Compensation Committee chair - \$5,000, Audit Committee member - \$4,000, Compensation Committee member - \$4,000, and Lead independent director - \$15,000.

STAND-ALONE GRANTS

From time to time our Board of Directors grants restricted stock or common share purchase options or warrants to selected directors, officers, employees and consultants as equity compensation to such persons on a stand-alone basis outside of any of our formal stock plans. The terms of these grants are individually negotiated.

On June 8, 2009, our board of directors approved the grant to Mr. Joyce of 4,000,000 shares of restricted common stock at a price per share of \$0.24, the vesting and issuance of which occurred in equal installments over a thirty-six-month period that commenced on June 30, 2010. Mr. Joyce may, from time to time, defer acceptance of the shares. However, all shares must be issued and accepted by Mr. Joyce by the expiration of the thirty-six-month vesting period. Mr. Joyce has accepted all 4,000,000 shares of the grant. However, the 600,000 shares previously accepted by Mr. Joyce were pledged as collateral for a loan and have been retained and/or sold by the lender and are no longer owned by Mr. Joyce.

In July 2013, our compensation committee and Board of Directors approved the issuance of four stock option grants to four of our executives. The options carried an exercise price of \$0.10 per share, have a ten year life and vest over the following schedule: 25% on July 1, 2014, 25% on July 1, 2015, 25% on July 1, 2016 and 25% on July 1, 2017. The numbers of shares underlying each of the stock option grants were as follows: 2,000,000 shares to our chief executive officer and 500,000 shares each to our president, chief science officer and chief financial officer.

AETHLON MEDICAL, INC. AND SUBSIDIARY**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****MARCH 31, 2014 AND 2013**

During the three months ended March 31, 2014, a former director exercised 182,927 in vested stock options through the contribution of \$2,000 in cash and \$13,000 in accrued expenses owed to him based on the exercise price of \$0.082 per share.

As of March 31, 2014, we have issued 22,568,158 options (of which 3,368,942 have been exercised or cancelled) and authorized the issuance of 4,000,000 shares of restricted stock outside of the 2005 Directors Compensation Plan, the 2012 Directors Compensation Plan, the 2000 Stock Option Plan, the 2003 Consultant Stock Plan and the 2010 Incentive Stock Plan.

In the fiscal year ended March 31, 2014, our Board of Directors granted, to our five outside directors, ten year options to acquire an aggregate of 1,595,536 shares of our common stock, all with an exercise price of \$0.082 per share.

The following is a summary of the stock options outstanding at March 31, 2014 and 2013 and the changes during the years then ended:

	Year Ended March 31,			
	2014		2013	
	Options	Weighted Average Exercise Price	Options	Weighted Average Exercise Price
Outstanding, beginning of year	21,095,798	\$ 0.28	19,428,693	\$ 0.31
Granted	5,220,536	\$ 0.09	1,667,105	\$ 0.08
Exercised	182,927	\$ 0.08	—	\$ —
Cancelled/Forfeited	—	\$ —	—	\$ —
Outstanding, end of year	26,133,407	\$ 0.25	21,095,798	\$ 0.28
Exercisable, end of year	22,487,563	\$ 0.27	19,141,625	\$ 0.29
Weighted average estimated fair value of options granted		\$ 0.13		\$ 0.08

The following outlines the significant weighted average assumptions used to estimate the fair value with respect to stock options utilizing the Binomial Lattice option pricing model for the years ended March 31, 2014 and March 31,

Explanation of Responses:

2013:

	Year Ended March 31,	
	2014	2013
Risk free interest rate	0.38% to 2.65%	1.44%
Average expected life	3 to 10 years	10 years
Expected volatility	91.05% to 102.67%	117.53%
Expected dividends	None	None

The detail of the options outstanding and exercisable as of March 31, 2014 is as follows:

Range of Exercise Prices	Options Outstanding			Options Exercisable	
	Number Outstanding	Weighted Average Remaining Life (Years)	Weighted Average Exercise Price	Number Outstanding	Weighted Average Exercise Price
\$0.08 - \$0.11	6,704,714	9.68 years	\$ 0.09	3,204,714	\$ 0.08
\$0.21 - \$0.25	11,207,143	4.28 years	\$ 0.24	11,061,299	\$ 0.24
\$0.36 - \$0.41	8,221,550	2.68 years	\$ 0.38	8,221,550	\$ 0.38
	26,133,407			22,487,563	

We recorded stock-based compensation expense related to share issuances and to options granted totaling \$607,946 and \$765,273 for the fiscal years ended March 31, 2014 and 2013, respectively. These expenses were recorded as stock compensation included in payroll and related expenses in the accompanying consolidated statement of operations for the years ended March 31, 2014 and 2013.

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AETHLON MEDICAL, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

MARCH 31, 2014 AND 2013

Our total stock-based compensation for fiscal years ended March 31, 2014 and 2013 included the following:

	March 31, 2014	March 31, 2013
Vesting of restricted stock grant	\$64,444	\$386,668
Incremental fair value of option modifications	1,914	23,027
Vesting of stock options	541,588	355,578
Total Stock-Based Compensation	\$607,946	\$765,273

As of March 31, 2014, we had \$270,952 of remaining unrecognized stock option expense, which is expected to be recognized over a weighted average remaining vesting period of 2.07 years.

On March 31, 2014, our stock options had a negative intrinsic value since the closing price on that date of \$0.17 per share was below the weighted average exercise price of our stock options.

7. RELATED PARTY TRANSACTIONS

DUE TO RELATED PARTIES

Certain of our officers and other related parties have advanced us funds, agreed to defer compensation and/or paid expenses on our behalf to cover working capital deficiencies. These unsecured and non-interest-bearing liabilities have been included as due to related parties in the accompanying consolidated balance sheets.

Other related party transactions are disclosed elsewhere in these notes to consolidated financial statements.

8. OTHER CURRENT LIABILITIES

Other current liabilities were comprised of the following items:

	March 31, 2014	March 31, 2013
Accrued interest	\$1,165,335	\$1,032,110
Accrued legal fees	179,465	179,465
Accrued liquidated damages	362,800	437,800
Other accrued liabilities	147,774	155,610
Total other current liabilities	\$1,855,374	\$1,804,985

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AETHLON MEDICAL, INC. AND SUBSIDIARY**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****MARCH 31, 2014 AND 2013****9. INCOME TAXES**

For the years ended March 31, 2014 and 2013, we had no income tax expense due to our net operating losses and 100% deferred tax asset valuation allowance.

At March 31, 2014 and 2013, we had net deferred tax assets as detailed below. These deferred tax assets are primarily composed of capitalized research and development costs and tax net operating loss carryforwards. Due to uncertainties surrounding our ability to generate future taxable income to realize these assets, a 100% valuation has been established to offset the net deferred tax assets.

Significant components of our net deferred tax assets at March 31, 2014 and 2013 are shown below:

	YEAR ENDED MARCH 31,	
	2014	2013
Deferred tax assets:		
Capitalized research and development	\$3,442,000	\$3,442,000
Net operating loss carryforwards	15,193,000	14,793,000
Total deferred tax assets	18,635,000	18,235,000
Total deferred tax liabilities	—	—
Net deferred tax assets	18,635,000	18,235,000
Valuation allowance for deferred tax assets	(18,635,000)	(18,235,000)
Net deferred tax assets	\$—	\$—

At March 31, 2014, we had tax net operating loss carryforwards for federal and state purposes approximating \$39 million and \$30 million, which begin to expire in the year 2020.

The provision for income taxes on earnings subject to income taxes differs from the statutory federal rate for the years ended March 31, 2014 and 2013 due to the following:

	2014	2013
Income taxes (benefit) at federal statutory rate of 34%	\$(4,541,000)	\$(1,663,000)
State income tax, net of federal benefit	(156,000)	(285,000)
Tax effect on non-deductible expenses and credits	4,297,000	215,000
Change in valuation allowance ¹	400,000	1,733,000
	\$-	\$-

Pursuant to Internal Revenue Code Sections 382, use of our tax net operating loss carryforwards may be limited.

ASC 740, "Income Taxes", clarifies the accounting for uncertainty in income taxes recognized in an entity's financial statements, and prescribes recognition thresholds and measurement attributes for financial statement disclosure of tax positions taken or expected to be taken on a tax return. Under ASC 740, the impact of an uncertain income tax position on the income tax return must be recognized at the largest amount that is more-likely-than-not to be sustained upon audit by the relevant taxing authority. An uncertain income tax position will not be recognized if it has less than a 50% likelihood of being sustained. Additionally, ASC 740 provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. Our practice is to recognize interest and/or penalties related to income tax matters in income tax expense. During the years ended March 31, 2014 and 2013, we did not recognize any interest or penalties relating to tax matters.

At and for the years ended March 31, 2014 and 2013, management does not believe the Company has any uncertain tax positions. Accordingly, there are no unrecognized tax benefits at March 31, 2014 or March 31, 2013.

Our tax returns for the years 2010 and forward are subject to examination by the Internal Revenue Service and 2009 and forward by the California Franchise Tax Board. We are currently not under examination by any taxing authorities.

AETHLON MEDICAL, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

MARCH 31, 2014 AND 2013

10. FAIR VALUE MEASUREMENTS

We follow FASB ASC 820, "FAIR VALUE MEASUREMENTS AND DISCLOSURES" ("ASC 820") in connection with financial assets and liabilities measured at fair value on a recurring basis subsequent to initial recognition.

ASC 820 requires that assets and liabilities carried at fair value will be classified and disclosed in one of the following three categories:

Level 1: Quoted market prices in active markets for identical assets or liabilities.

Level 2: Observable market based inputs or unobservable inputs that are corroborated by market data.

Level 3: Unobservable inputs that are not corroborated by market data.

The hierarchy noted above requires us to minimize the use of unobservable inputs and to use observable market data, if available, when determining fair value.

The fair value of our recorded derivative liabilities is determined based on unobservable inputs that are not corroborated by market data, which is a Level 3 classification. We record derivative liabilities on our balance sheet at fair value with changes in fair value recorded in our consolidated statements of operations. Our fair value measurements at the reporting date were as follows:

At March 31, 2014:

Explanation of Responses:

Description	Quoted Prices in	Active Markets for Identical Assets	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	(Level 1)			
Derivative Liabilities	\$ -	\$ -	\$ -	\$ 10,679,067
Total Assets	\$ -	\$ -	\$ -	\$ 10,679,067

At March 31, 2013:

Description	Quoted Prices in	Active Markets for Identical Assets	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	(Level 1)			
Derivative Liabilities	\$ -	\$ -	\$ -	\$ 3,588,239
Total Assets	\$ -	\$ -	\$ -	\$ 3,588,239

The following outlines the significant weighted average assumptions used to estimate the fair value information presented for the fiscal years ended March 31, 2014 and 2013, in connection with our April 2011 convertible note, July & August 2011 10% convertible notes and the September 2011 convertible note offerings and with respect to warrant and embedded conversion option derivative instruments utilizing the Binomial Lattice option pricing model:

Fiscal Year Ended March 31, 2014

Risk free interest rate	0.02% - 0.79%
Average expected life	0.25 – 2.8 years
Expected volatility	58.0% - 103.1%
Expected dividends	None

Fiscal Year Ended March 31, 2013

Risk free interest rate	0.05% - 1.56%
Average expected life	0.25 – 3.6 years

Explanation of Responses:

Expected volatility 76.0% - 107.1%
 Expected dividends None

The table below sets forth a summary of changes in the fair value of our Level 3 financial instruments for the year ended March 31, 2014:

	April 1, 2013	Recorded New Derivative Liabilities	Change in estimated fair value recognized in results of operations	Reclassification of Derivative Liability to Paid in capital	March 31, 2014
Derivative liabilities	\$3,588,239	\$ -	\$5,729,780	\$ 1,361,048	\$10,679,067

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AETHLON MEDICAL, INC. AND SUBSIDIARY**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****MARCH 31, 2014 AND 2013**

The table below sets forth a summary of changes in the fair value of our Level 3 financial instruments for the year ended March 31, 2013:

	April 1,	Recorded New Derivative	Change in estimated fair value recognized in results of operations	Reclassification of Derivative Liability to Paid in capital	March 31, 2013
Derivative liabilities	\$3,588,615	\$ —	\$ (44,705)	\$ 44,329	\$3,588,239

11. DARPA CONTRACT AND RELATED REVENUE RECOGNITION

As discussed in Note 1, we entered into a contract with the DARPA on September 30, 2011. Under the DARPA award, we have been engaged to develop a therapeutic device to reduce the incidence of sepsis, a fatal bloodstream infection that often results in the death of combat-injured soldiers. The award from DARPA was a fixed-price contract with potential total payments to us of \$6,794,389 over the course of five years. Fixed price contracts require the achievement of multiple, incremental milestones to receive the full award during each year of the contract. Under the terms of the contract, we will perform certain incremental work towards the achievement of specific milestones against which we will invoice the government for fixed payment amounts.

Originally, only the base year (year one contract) was effective for the parties, however, DARPA subsequently exercised the option on the second and third years of the contract. DARPA has the option to enter into the contract for years four and five. The milestones are comprised of planning, engineering and clinical targets, the achievement of which in some cases will require the participation and contribution of third party participants under the contract. There can be no assurance that we alone, or with third party participants, will meet such milestones to the satisfaction of the government and in compliance with the terms of the contract or that we will be paid the full amount of the contract revenues during any year of the contract term. We commenced work under the contract in October 2011.

Due to budget restrictions within the Department of Defense, on February 10, 2014, DARPA reduced the scope of our contract in years three through five of the contract. The reduction in scope focused our research on exosomes, viruses and blood processing instrumentation. This scope reduction will reduce the possible payments under the contract by \$858,491 over years three through five. We recently completed a rebudgeting of the expected costs on the remaining years of the DARPA contract based on the reduced milestones and have concluded that the reductions in our costs due to the scaled back level of work will almost entirely offset the anticipated revenue levels based on current assumptions.

Fiscal Year Ended March 31, 2014

As a result of achieving eight milestones in the fiscal year ended March 31, 2014, we reported \$1,466,482 in contract revenue for that fiscal year. The details of the eight milestones achieved during the fiscal year ended March 31, 2014 were as follows:

Milestone 2.3.2.2 – Formulate initial design work based on work from the previous phase. Begin to build and test selected instrument design and tubing sets. The milestone payment was \$195,581. Management considers this milestone to be substantive as it was not dependent on the passage of time nor was it based solely on another party's efforts. We demonstrated that we were able to formulate the initial design work and to build and test selected instrument design and tubing sets as part of our submission for approval. The report was accepted by the contracting officer's representative and the invoice was submitted thereafter.

Milestone 2.3.2.2 – Write and test software and conduct ergonomic research. Begin discussions with the systems integrator. The milestone payment was \$195,581. Management considers this milestone to be substantive as it was not dependent on the passage of time nor was it based solely on another party's efforts. We obtained wrote and tested software and conducted ergonomic research and began discussions with the systems integrator. The report was accepted by the contracting officer's representative and the invoice was submitted thereafter.

Milestone 2.3.3.2 – Cartridge construction with optimized affinity matrix design for each potential target. Complete the capture agent screening. The milestone payment was \$208,781. Management considers this milestone to be substantive as it was not dependent on the passage of time nor was it based solely on another party's efforts. We completed the cartridge construction with optimized affinity matrix design for each potential target and completed the capture agent screening. The report was accepted by the contracting officer's representative and the invoice was submitted thereafter.

AETHLON MEDICAL, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

MARCH 31, 2014 AND 2013

Milestone M5 – Target capture > 90% in 24 hours for at least three targets in blood or blood components. The milestone payment was \$208,781. Management considers this milestone to be substantive as it was not dependent on the passage of time nor was it based solely on another party's efforts. We demonstrated that we were able to capture > 90% in 24 hours for at least three of the agreed targets in blood or blood components. The report was accepted by the contracting officer's representative and the invoice was submitted thereafter.

Milestone M3 – Conduct a series of experiments aimed at characterizing the contribution of several alternate fluidic designs and methods of perfusing plasma filters and affinity columns in the performance of affinity plasmapheresis. The milestone payment was \$195,576. Management considers this milestone to be substantive as it was not dependent on the passage of time nor was it based solely on another party's efforts. We demonstrated that we had conducted the relevant series of experiments. The report was accepted by the contracting officer's representative and the invoice was submitted thereafter.

Milestone 2.4.2.1 – Evaluate contribution of manufacturing process variables to binding capacity of affinity resin. The milestone payment was \$197,362. Management considers this milestone to be substantive as it was not dependent on the passage of time nor was it based solely on another party's efforts. We demonstrated that we had evaluated the contribution of manufacturing process variables to binding capacity of affinity resin. The report was accepted by the contracting officer's representative and the invoice was submitted thereafter.

Milestone 2.4.1.1 – Design and fabricate optimized configuration(s) of hemopurification device(s) that contain(s) a combination of hemofilters, plasma filters and affinity columns. The milestone payment was \$186,164. Management considers this milestone to be substantive as it was not dependent on the passage of time nor was it based solely on another party's efforts. We demonstrated that we had designed and fabricated optimized configuration of hemopurification devices. The report was accepted by the contracting officer's representative and the invoice was submitted thereafter.

Milestone 2.4.2.3 – Perform biocompatibility tests for the combination ADAPT device to confirm the combination cartridge does not present additional risk. The milestone payment was \$78,641. Management considers this milestone to be substantive as it was not dependent on the passage of time nor was it based solely on another party's efforts. We demonstrated that we had performed biocompatibility tests for the combination ADAPT device to confirm the combination cartridge does not present additional risk. The report was accepted by the contracting officer's representative and the invoice was submitted thereafter.

Fiscal Year Ended March 31, 2013

As a result of achieving six milestones in the fiscal year ended March 31, 2013, we reported \$1,230,004 in contract revenue for that fiscal year. The details of the six milestones achieved during the fiscal year ended March 31, 2013 were as follows:

Milestone 2.2.2.3 – Perform preliminary quantitative real time PCR to measure viral load, and specific DNA or RNA targets. The milestone payment was \$216,747. Management considers this milestone to be substantive as it was not dependent on the passage of time nor was it based solely on another party's efforts. We demonstrated that we were able to measure viral load of one or more targets as part of our submission for approval. The report was accepted by the contracting officer's representative and the invoice was submitted thereafter.

Milestone 2.2.1.4 – Obtain all necessary IRB documentation and obtain both institutional and Government approval in accordance with IRB documentation submission guidance prior to conducting human or animal testing. The milestone payment was \$183,367. Management considers this milestone to be substantive as it was not dependent on the passage of time nor was it based solely on another party's efforts. We obtained all of the required documentation from both institutional and Government authorities. The report was accepted by the contracting officer's representative and the invoice was submitted thereafter.

Milestone M2 – Target capture > 50% in 24 hours for at least one target in blood or blood components. The milestone payment was \$216,747. Management considers this milestone to be substantive as it was not dependent on the passage of time nor was it based solely on another party's efforts. We demonstrated that we were able to capture > 50% in 24 hours of one of the agreed targets in blood or blood components. The report was accepted by the contracting officer's representative and the invoice was submitted thereafter.

Milestone 2.3.3.1 – Build the ADAPT capture cartridges with the identified affinity agents. Measure the rate of capture of the specific targets from in ex vivo recirculation experiments from cell culture and blood. The milestone payment was \$208,781. Management considers this milestone to be substantive as it was not dependent on the passage of time nor was it based solely on another party's efforts. We demonstrated that we were able build the ADAPT capture cartridges with the identified affinity agents and to measure the rate of capture of the specific targets from in ex vivo recirculation experiments from cell culture and blood. The report was accepted by the contracting officer's representative and the invoice was submitted thereafter.

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AETHLON MEDICAL, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

MARCH 31, 2014 AND 2013

Milestone 2.3.2.1 – Demonstrate the effectiveness of the prototype device in vivo in animals preventing platelet activation or clotting in at least a 2 hour blood pumping experiment at 75 mL/min blood flow. The milestone payment amount was \$195,581. Management considers this milestone to be substantive as it was not dependent on the passage of time nor was it based solely on another party's efforts. The prototype device was successfully used in vivo in animals preventing platelet activation or clotting in at least a 2 hour blood pumping experiment at 75 mL/min blood flow. The report was accepted by the contracting officer's representative and the invoice was submitted thereafter.

Milestone M4 – Target capture > 50% in 24 hours for at least 5 targets in blood or blood components. The milestone payment was \$208,781. Management considers this milestone to be substantive as it was not dependent on the passage of time nor was it based solely on another party's efforts. We demonstrated that we were able to capture > 50% in 24 hours for at least 5 of the agreed targets in blood or blood components. The report was accepted by the contracting officer's representative and the invoice was submitted thereafter.

12. SIGNIFICANT FOURTH QUARTER ADJUSTMENTS

During the fourth quarter of the fiscal years ended March 31, 2014 and 2013, we did not deem any unusual or infrequently occurring items or adjustments to be material to our fourth quarter results.

13. COMMITMENTS AND CONTINGENCIES

EMPLOYMENT CONTRACTS

We entered into an employment agreement with our Chairman of the Board (“Chairman”) effective April 1, 1999. The agreement, which is cancelable by either party upon sixty days’ notice, will be in effect until the Chairman retires or ceases to be employed by us. Under the terms of the agreement, if the Chairman is terminated he may become eligible to receive a salary continuation payment in the amount of at least twelve months' base salary, which was increased to \$350,000 per year in June 2014.

We entered into an employment agreement with Dr. Tullis ("Tullis") effective January 10, 2000 as our Chief Science Officer ("CSO"). Under the terms of the agreement, if Tullis is terminated he may become eligible to receive a salary continuation payment in the amount of twelve months base salary, which is \$195,000 per year.

LEASE COMMITMENTS

We currently rent approximately 2,300 square feet of executive office space at 8910 University Center Lane, Suite 660, San Diego, CA 92122 at the rate of \$6,475 per month on a four year lease that expires in September 2014. We also rent approximately 1,700 square feet of laboratory space at 11585 Sorrento Valley Road, Suite 109, San Diego, California 92121 at the rate of \$2,917 per month on a two year lease that expires in October 2014. We are currently searching for new space in the greater San Diego area.

Our Exosome Sciences, Inc. subsidiary rents approximately 2,055 square feet of office and laboratory space at 11 Deer Park Drive, South Brunswick, NJ at the rate of \$3,425 per month on a one year lease that expires in October 2014. Our current plans are to renew the lease prior to expiration.

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AETHLON MEDICAL, INC. AND SUBSIDIARY**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****MARCH 31, 2014 AND 2013**

Rent expense approximated \$163,000 and \$123,000 for the fiscal years ended March 31, 2014 and 2013, respectively. As of March 31, 2014, commitments under the lease agreements are as follows:

	2015
8910 University Center Lane, Suite 660, San Diego, CA 92122 office lease	\$43,795
11585 Sorrento Valley Road, Suite 109, San Diego, California 92121 office lease	22,755
11 Deer Park Drive, South Brunswick, NJ	23,975
Total Lease Commitments	\$90,525

LEGAL MATTERS

From time to time, claims are made against us in the ordinary course of business, which could result in litigation. Claims and associated litigation are subject to inherent uncertainties and unfavorable outcomes could occur, such as monetary damages, fines, penalties or injunctions prohibiting us from selling one or more products or engaging in other activities.

The occurrence of an unfavorable outcome in any specific period could have a material adverse effect on our results of operations for that period or future periods. Other than as mentioned here, we are not presently a party to any pending or threatened legal proceedings.

On February 24, 2014, we entered into a Settlement Agreement and General Release (the "Settlement Agreement") with Gemini Master Fund, Ltd., a Cayman Islands company ("Gemini"), which, among other things, resulted in the dismissal with prejudice of the complaint filed by Gemini against us on July 5, 2012 in the Supreme Court of the State of New York, County of New York, entitled Gemini Master Fund Ltd. v. Aethlon Medical, Inc., Index No. 652358/2012 (the "Complaint").

In the Complaint, Gemini sought relief both in the form of money damages and delivery of shares of our common stock. The Complaint alleged, among other things, that we were in default of a convertible promissory note ("Convertible Note") originally issued to Gemini on February 12, 2010 by failing to pay the Convertible Note in full and by failing to honor certain requests by Gemini to convert the principal and interest under the Convertible Note into shares of our common stock. The Complaint also alleged that we failed to issue shares upon the presentation of exercise notices under warrants originally issued to Gemini in 2009 and 2010 (respectively, the "2009 Warrant" and the "2010 Warrant").

In the Complaint, Gemini alleged it was entitled to 22,389,382 shares of common stock upon conversion of the balance of the Convertible Note and Gemini alleged that it was entitled to receive 30,370,814 shares of common stock pursuant to the 2009 Warrant and the 2010 Warrant, for a combined sum of 52,760,196 common shares.

In response, we provided documentation that the Convertible Note had been paid in full in cash and accepted by Gemini prior to the filing of the Complaint. In addition, we had maintained on our books the total number of shares required to be issued under the 2009 Warrant, the 2010 Warrant and the 2008 Warrant (defined below) combined was 6,359,999 shares.

The Settlement Agreement required us to issue a total of 7,522,854 shares of common stock into an escrow and those shares were to be released to Gemini ratably over a ten-month period. The shares were issued upon partial exercise of the 2009 Warrant and 2010 Warrant as well as under a third warrant, issued by us to Gemini in 2008 (the "2008 Warrant"). No shares were issued as consideration for the alleged default under the Convertible Note or in consideration of the releases granted in the Settlement Agreement. In addition, our insurance company paid Gemini \$150,000 in cash. Upon the completion of the share issuances, the 2008 Warrant, the 2009 Warrant and the 2010 Warrants were canceled. In addition, under the Settlement Agreement, the Convertible Note (and any other agreement to pay Gemini or issue stock or anything else of value to Gemini) was extinguished and fully satisfied.

As we previously had 6,359,999 shares of common stock reserved for issuance under the three Warrants described above, the settlement increased our fully diluted shares outstanding by 1,162,855 shares.

Following the performance of the settlement terms described above, a Stipulation of Dismissal was filed with the Court, permanently terminating the litigation. The Settlement Agreement also provided for mutual and full releases of all other claims between Gemini and us.

The Company accrued an estimate of \$1,000,000 for such matter at December 31, 2013 and expensed such amount during the quarter ended December 31, 2013. Upon final settlement, management determined that the expense was approximately \$583,000. Accordingly, during the fourth quarter of the year ended March 31, 2014, the Company recorded a credit to expense of approximately \$417,000 related to this matter.

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AETHLON MEDICAL, INC. AND SUBSIDIARY**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****MARCH 31, 2014 AND 2013**

14. SEGMENTS

We operate our businesses principally through two reportable segments: Aethlon, which represents our therapeutic business activities, and ESI, which represents our diagnostic business activities. Our reportable segments have been determined based on the nature of the potential products being developed. ESI did not have any operations in the fiscal year ended March 31, 2013.

Aethlon's revenue is generated primarily from government contracts to date and ESI does not yet have any revenues. We have not included any allocation of corporate overhead to the ESI segment.

The following tables set forth certain information regarding our segments and other operations that conforms to the consolidated balance sheet and statement of operations presented in this Report:

	Fiscal Years Ended March	
	31,	
	2014	2013
Revenues:		
Aethlon	\$1,623,769	\$1,230,004
ESI	—	—
Total Revenues	\$1,623,769	\$1,230,004
Operating Losses:		
Aethlon	\$(2,651,863)	\$(3,575,354)
ESI	(404,065)	—
Total Operating Loss	\$(3,055,928)	\$(3,575,354)
Net Losses:		
Aethlon	\$(13,357,232)	\$(4,892,040)
ESI	(81,730)	—
Net Loss Before Non-Controlling Interests	\$(13,438,962)	\$(4,892,040)

Cash:

Explanation of Responses:

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Aethlon	\$ 208,259	\$ 125,274
ESI	1,042,020	–
Total Cash	\$ 1,250,279	\$ 125,274
Total Assets:		
Aethlon	\$ 597,026	\$ 496,694
ESI	1,098,076	–
Total Assets	\$ 1,695,102	\$ 496,694
Capital Expenditures:		
Aethlon	\$ 37,313	\$–
ESI	58,743	–
Capital Expenditures	\$ 96,056	\$–
Depreciation and Amortization:		
Aethlon	\$ 11,549	\$ 10,484
ESI	9,538	–
Total Depreciation and Amortization	\$ 21,087	\$ 10,484
Interest Expense:		
Aethlon	\$ 1,282,638	\$ 1,132,314
ESI	4,583	–
Total Interest Expense	\$ 1,287,221	\$ 1,132,314

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AETHLON MEDICAL, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

MARCH 31, 2014 AND 2013

15. SUBSEQUENT EVENTS (UNAUDITED)

Management has evaluated events subsequent to March 31, 2014 through the date that the accompanying condensed consolidated financial statements were filed with the Securities and Exchange Commission for transactions and other events which may require adjustment of and/or disclosure in such financial statements.

Government Contracts

Subsequent to March 31, 2014, we billed \$197,362 under our DARPA contract and billed \$62,696 under the Battelle subcontract and we collected \$135,376 under both contracts.

Common Stock Issuances

Subsequent to March 31, 2014, we issued 219,127 shares of common stock pursuant to our S-8 registration statement covering our Amended 2010 Stock Plan at an average price of \$0.17 per share in payment for internal controls, legal and scientific consulting services valued at \$38,268 based on the value of the services provided.

Subsequent to March 31, 2014, we completed unit subscription agreements with seven accredited investors (the "Purchasers") pursuant to which the Purchasers purchased an aggregate of \$320,800 of restricted common stock at an average price of \$0.15 per share. The common stock purchase price under the subscription agreement was determined to be 80% of the average closing price of our common stock for the five-day period immediately preceding the date of each subscription agreement, resulting in the issuance of 2,192,444 shares of common stock.

Each Purchaser also received one common stock purchase warrant for each two shares of common stock purchased under his subscription agreement. The warrant exercise price was calculated based upon 120% of the average of the closing prices of our common stock for the five-day period immediately preceding the parties entering into their

subscription agreement.

Stock Option Grants

On June 6, 2014, our Board of Directors approved the following grants of options to certain officers and directors of the Company:

To Mr. James A. Joyce, an option to acquire an aggregate of 1,500,000 shares of our common stock at an exercise price of \$0.19 per share, the closing price of our common stock on the date of grant. The option vested as to 500,000 shares on the grant date and will vest as to an additional 500,000 shares on each of the first two anniversaries of the grant date. Unless earlier exercised or terminated, the option will expire June 6, 2024.

To Mr. Rodney S. Kenley, an option to acquire an aggregate of 250,000 shares of our common stock at an exercise price of \$0.19 per share, the closing price of our common stock on the date of grant. The option vested as to 83,333 shares on the grant date and will vest as to an additional 83,333 shares on the first anniversary of the grant date and 83,334 shares on the second anniversary of the grant date. Unless earlier exercised or terminated, the option will expire June 6, 2024.

To Mr. James B. Frakes, an option to acquire an aggregate of 250,000 shares of our common stock at an exercise price of \$0.19 per share, the closing price of our common stock on the date of grant. The option vested as to 83,333 shares on the grant date and will vest as to an additional 83,333 shares on the first anniversary of the grant date and 83,334 shares on the second anniversary of the grant date. Unless earlier exercised or terminated, the option will expire June 6, 2024.

Changes to 2012 Board Compensation Program

In July 2012, the Board approved a Board Compensation Program (the “2012 Program”), which modified and superseded the 2005 Directors Compensation Program that had been in effect previously. On June 6, 2014, the Board approved certain changes to the 2012 Program. Under the modified 2012 Program, in which only non-employee Directors may participate, a new eligible Director will receive an initial grant of \$50,000 worth of options to acquire shares of common stock, with such grant being valued at the exercise price based on the average of the closing bid prices of our common stock for the five trading days preceding the first day of the fiscal year. These options will have a term of ten years and will vest 1/3 upon grant and 1/3 upon each of the first two anniversaries of the date of grant.

At the beginning of each fiscal year, each existing Director eligible to participate in the 2012 Program also will receive a grant of \$35,000 worth of options valued at the exercise price based on the average of the closing bid prices of the Common Stock for the five trading days preceding the first day of the fiscal year. Such options will vest on the first anniversary of the date of grant. In lieu of per meeting fees, under the 2012 Program eligible Directors will

receive an annual Board retainer fee of \$30,000. The modified 2012 Program also provides for the following annual retainer fees: Audit Committee Chair - \$5,000, Compensation Committee chair - \$5,000, Audit Committee member - \$4,000, Compensation Committee member - \$4,000 and Lead independent director - \$15,000.

All of the foregoing actions - the changes in base salaries, the option grants and the changes to the Directors Compensation Program discussed herein - were approved and recommended by the Company's Compensation Committee prior to approval by the Board.

Convertible Notes Payable – See Note 16 below

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AETHLON MEDICAL, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

MARCH 31, 2014 AND 2013

NOTE 16 – PRO FORMA BALANCE SHEET (UNAUDITED)

Management has presented unaudited pro forma balance sheet information as if the subsequent events discussed below had occurred on March 31, 2014. Such pro forma information is subject to future adjustment as management determines the final accounting for such transactions.

Weiner Note Conversion

On June 24, 2014, we entered into an agreement with the Ellen R. Weiner Family Revocable Trust (the “Trust”), a holder of a Series A 12% Convertible Note (the “Note”) (see Note 5), which previously was classified as being in default. As per the agreement, the Trust converted a past due combined principal and interest balance of \$1,003,200 into restricted common stock.

Additionally, the Trust agreed to waive anti-dilution price protection underlying warrants previously issued to the Trust. On June 26, 2014, three other parties who held similar warrants also agreed to waive their anti-dilution price protection. As a result of the debt conversion and elimination of warrant anti-dilution price protection, \$3.7 million of our previously classified derivative liability will convert into equity based on the fair value of securities on our fiscal year-end date of March 31, 2014.

As a result of the note conversion and derivative liability reclassification into equity, our balance sheet equity will increase by approximately \$4.7 million.

Under its agreement, the Trust converted the entire \$1,003,200 past due principal and interest balance on the Note, which previously was in default, into an aggregate of 23,318,254 restricted shares of our common stock and five-year warrants to acquire up to 6,809,524 shares of our common stock at an exercise price of \$.042 per share and up to 397,222 shares of our common stock at an exercise price of \$.108 per share (collectively, the “Conversion Securities”).

In exchange for the Trust's conversion in full of the Note and accrued interest and for the waivers of anti-dilution price protection in the previously issued warrants, in addition to the Conversion Securities, we issued to the Trust 75,000 restricted shares of common stock as a service fee, changed the exercise price of all of the previously issued warrants to \$.042 per share and extended the expiration date of all of the previously issued warrants to July 1, 2018.

Bird Estate Extension

On July 8, 2014, we entered into a restructuring agreement (the "Agreement") with the Estate of Allan Bird (the "Estate"), a holder of a Series A 12% Convertible Note (the "Note"), which previously was classified as being in default. In the Agreement, the Estate agreed to extend the expiration date of the Note to April 1, 2016, to convert approximately \$116,970 of accrued interest to equity, and to waive anti-dilution price protection underlying the Note and warrants previously issued to the Estate.

As a result of the waiver of all anti-dilution price protection by the Estate, we will reclassify to equity \$1,238,292 from derivative liability.

Also, the execution of the Agreement results in the waiver of anti-dilution price protection under agreements with three other note and warrant holders, which will cause an additional \$5,724,761 of derivative liability to be reclassified from liability to equity.

In addition, as a result of a note conversion and waiver of anti-dilution price protection previously reported on Form 8-K on June 30, 2014, a combined \$4,719,214 of principal, accrued interest and derivative liability has been reclassified into equity.

Based on the Agreement, the elimination of antidilution provisions and the note and accrued interest conversions, all previously reported derivative liabilities will be reclassified into equity.

Under the Agreement, the Estate converted the entire \$116,970 past due interest balance on the Note, which previously was in default, into an aggregate of 2,591,846 restricted shares of our common stock. The Estate received five-year warrants to acquire up to 2,321,429 shares of our common stock at an exercise price of \$.042 per share (which exercise price was the result of certain contractual price adjustments previously made during 2011). Based on our common stock prices during a period of negotiation with the Estate including during calendar year 2013, the Estate also received five-year warrants to acquire up to 135,417 shares of our common stock at an exercise price of \$.108 (collectively known as the "Conversion Securities").

In exchange for the Estate's extension of the Note, conversion of accrued interest and for the waivers of anti-dilution price protection in the previously issued warrants, in addition to the Conversion Securities, we also issued to the Estate 25,000 restricted shares of common stock as a service fee and extended the expiration date of all of the previously issued warrants to July 1, 2018.

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AETHLON MEDICAL, INC. AND SUBSIDIARY**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****MARCH 31, 2014 AND 2013**

Pro Forma References

The unaudited pro forma balance sheet information as of March 31, 2014 assumes (1) conversion of one of the Amended and Restated Series A 12% Convertible Notes (the Trust Note) in the principal amount of \$660,000 as well as \$343,200 of related accrued interest into 23.3 million shares of common stock, (2) the extension of the other Amended and Restated Series A 12% Convertible Note (the Estate Note) and conversion of \$116,970 of related accrued interest into 2.6 million shares of common stock, (3) reduction of accrued interest balance by \$85,800 for the Trust Note and by \$29,280 for the Estate Note, (4) the waiver of price antidilution protection on certain warrants in exchange for an extension on those warrants with a corresponding fair value change based on June 24, 2014 inputs of \$96,469 for the Trust warrant extension and based on July 8, 2014 inputs of \$29,679 for the Estate warrants, (5) the reclassification of \$10,679,067 of our derivative liability into paid in capital based upon the fair value of those derivatives at March 31, 2014, (6) calculation of a loss on the payment of shares and warrants as part of the conversion of accrued interest with an estimated fair value of \$1,876,421 to the Trust and \$665,571 to the Estate, and (7) the payment of 75,000 restricted shares of common stock to the Trust as a fee, valued at \$12,000 and the payment of 25,000 restricted shares of common stock, valued at \$4,250.

The following unaudited pro forma information has been prepared as though these subsequent event transactions had occurred on March 31, 2014. The pro forma references refer to the above paragraph.

	Aethlon Medical, Inc. Consolidated		Pro Forma Consolidated	
	Balance Sheet	Pro Forma Adjustments		Balance Sheet
	March 31, 2014	Amount	Reference	March 31, 2014
ASSETS				
CURRENT ASSETS				
Cash	\$ 1,250,279	\$-		\$ 1,250,279
Accounts receivable	95,177	-		95,177
Deferred financing costs	83,191	-		83,191
Prepaid expenses	50,699	-		50,699

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TOTAL CURRENT ASSETS	1,479,346	–		1,479,346
NON-CURRENT ASSETS				
Property and equipment, net	84,279	–		84,279
Patents, net	112,489	–		112,489
Deposits	18,988	–		18,988
TOTAL NONCURRENT ASSETS	215,756	–		215,756
TOTAL ASSETS	\$ 1,695,102	\$–		\$ 1,695,102
LIABILITIES AND DEFICIT				
CURRENT LIABILITIES				
Accounts payable	\$ 517,651	\$–		\$ 517,651
Due to related parties	839,070			839,070
Notes payable, net	390,000			390,000
Convertible notes payable, current portion	1,367,655	(885,000)	(1) & (2)	482,655
Derivative liabilities	10,679,067	(10,679,067)	(5)	–
Other current liabilities	1,855,374	(575,250)	(1), (2) & (3)	1,280,124
TOTAL CURRENT LIABILITIES	15,648,817	(12,139,317)		3,509,500
NONCURRENT LIABILITIES				
Convertible notes payable, non-current portion	776,451	225,000	(2)	1,001,451
TOTAL NONCURRENT LIABILITIES	776,451	225,000		1,001,451
TOTAL LIABILITIES	16,425,268	(11,914,317)		4,510,951
COMMITMENTS AND CONTINGENCIES				
STOCKHOLDERS' DEFICIT				
Common stock	224,984	26,010	(1), (5), (6) & (7)	250,994
Additional paid in capital	59,659,137	14,457,617	(1), (4), (5), (6) & (7)	74,116,754
Accumulated deficit	(74,832,557)	(2,569,310)	(2), (3), (4), (5), (6) & (7)	(77,401,867)
TOTAL AETHLON MEDICAL, INC. STOCKHOLDERS' DEFICIT	(14,948,436)	11,914,317		(3,034,119)
Noncontrolling interests	218,270	–		218,270
TOTAL DEFICIT	(14,730,166)	11,914,317		(2,815,849)
TOTAL LIABILITIES AND DEFICIT	\$ 1,695,102	\$–		\$ 1,695,102

AETHLON MEDICAL, INC. AND SUBSIDIARY

CONDENSED CONSOLIDATED BALANCE SHEETS

	September 30, 2014 (Unaudited)	March 31, 2014
ASSETS		
Current assets		
Cash	\$526,187	\$1,250,279
Accounts receivable	258,672	95,177
Deferred financing costs	66,189	83,191
Prepaid expenses and other current assets	41,141	50,699
Total current assets	892,189	1,479,346
Property and equipment, net	70,185	84,279
Patents and patents pending, net	107,907	112,489
Deposits	18,988	18,988
Total assets	\$1,089,269	\$1,695,102
LIABILITIES AND STOCKHOLDERS' DEFICIT		
Current liabilities		
Accounts payable	\$609,153	\$517,651
Due to related parties	888,778	839,070
Notes payable	190,000	390,000
Convertible notes payable, current portion	483,421	1,367,655
Derivative liabilities	-	10,679,067
Other current liabilities	1,216,604	1,855,374
Total current liabilities	3,387,956	15,648,817
Noncurrent liabilities		
Convertible notes payable, noncurrent portion	990,520	776,451
Total noncurrent liabilities	990,520	776,451
Total liabilities	4,378,476	16,425,268
Commitments and Contingencies (Note 13)		
Stockholders' Deficit		
Common stock, par value \$0.001 per share; 500,000,000 shares authorized as of September 30, 2014 and March 31, 2014; 262,713,781 and 224,973,980 shares issued and outstanding as of September 30, 2014 and March 31, 2014, respectively	262,712	224,984

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Additional paid-in capital	75,654,853	59,659,137
Accumulated deficit	(79,335,907)	(74,832,557)
Total Aethlon Medical, Inc. stockholders' deficit before noncontrolling interests	(3,418,342)	(14,948,436)
Noncontrolling interests	129,135	218,270
Total deficit	(3,289,207)	(14,730,166)
Total liabilities and deficit	\$ 1,089,269	\$ 1,695,102

See accompanying notes.

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AETHLON MEDICAL, INC. AND SUBSIDIARY

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

For the Three and Six Month Periods Ended September 30, 2014 and 2013

(Unaudited)

	Three Months Ended September 30, 2014	Three Months Ended September 30, 2013	Six Months Ended September 30, 2014	Six Months Ended September 30, 2013
REVENUES				
Government contract revenue	\$479,075	\$644,887	\$530,371	\$840,483
OPERATING EXPENSES				
Professional fees	308,821	327,511	710,434	651,581
Payroll and related expenses	544,354	404,849	1,165,040	863,480
General and administrative	227,092	142,323	428,097	339,014
Total operating expenses	1,080,267	874,683	2,303,571	1,854,075
OPERATING LOSS	(601,192)	(229,796)	(1,773,200)	(1,013,592)
OTHER EXPENSE				
Loss on debt conversion	65,493	17,467	2,531,123	40,256
(Gain)/loss on change in fair value of derivative liability	–	2,992,002	–	2,382,877
Interest and other debt expenses	78,145	110,405	144,799	216,443
Loss on extension of warrants	143,363	–	143,363	–
Total other expense	287,001	3,119,874	2,819,285	2,639,576
NET LOSS BEFORE NONCONTROLLING INTERESTS	(888,193)	(3,349,670)	(4,592,485)	(3,653,168)
LOSS ATTRIBUTABLE TO NONCONTROLLING INTERESTS	(40,784)	–	(89,135)	–
NET LOSS ATTRIBUTABLE TO COMMON STOCKHOLDERS	\$(847,409)	\$(3,349,670)	\$(4,503,350)	\$(3,653,168)
BASIC AND DILUTED LOSS PER COMMON SHARE	\$(0.00)	\$(0.02)	\$(0.02)	\$(0.02)

Explanation of Responses:

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WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING – BASIC AND DILUTED	259,369,911	187,643,582	243,494,916	182,004,220
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See accompanying notes.

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AETHLON MEDICAL, INC. AND SUBSIDIARY

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

For the Six Months Ended September 30, 2014 and 2013

(Unaudited)

	Six Months Ended September 30, 2014	Six Months Ended September 30, 2013
Cash flows from operating activities:		
Net loss	\$(4,592,485)	\$(3,653,168)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	18,676	4,727
Stock based compensation	260,680	190,601
Fair market value of common stock, warrants and options issued for services	162,358	264,343
Change in fair value of derivative liabilities	–	2,382,877
Loss on extension of warrants	143,363	–
Loss on debt conversion	2,531,123	40,256
Amortization of debt discount and deferred financing costs	21,502	4,578
Changes in operating assets and liabilities:		
Accounts receivable	(162,495)	(11,404)
Prepaid expenses and other current assets	9,558	(25,202)
Accounts payable and other current liabilities	163,646	(33,170)
Due to related parties	49,708	91,042
Net cash used in operating activities	(1,394,366)	(744,520)
Cash flows from financing activities:		
Proceeds from the issuance of notes payable	–	400,000
Proceeds from the issuance of common stock	670,274	228,000
Net cash provided by financing activities	670,274	628,000
Net decrease in cash	(724,092)	(116,520)
Cash at beginning of period	1,250,279	125,274
Cash at end of period	\$526,187	\$8,754

See accompanying notes.

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AETHLON MEDICAL, INC. AND SUBSIDIARY

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (CONTINUED)

For the Six Months Ended September 30, 2014 and 2013

(Unaudited)

	Six Months Ended September 30, 2014	Six Months Ended September 30, 2013
Supplemental disclosures of cash flow information:		
Cash paid during the period for:		
Interest	\$-	\$-
Supplemental disclosures of non-cash investing and financing activities:		
Debt and accrued interest converted to common stock	\$1,007,631	\$420,460
Reclassification of warrant derivative liability into equity	\$10,679,067	\$106,501
Reclassification of accounts payable to convertible notes payable	\$-	\$47,000
Deferred financing costs recorded in connection with debt amendment	\$5,000	\$-
Reclassification of accrued interest to convertible notes payable	\$25,766	\$20,027

See accompanying notes.

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AETHLON MEDICAL, INC. AND SUBSIDIARY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

September 30, 2014

1. NATURE OF BUSINESS AND BASIS OF PRESENTATION

ORGANIZATION

Aethlon Medical, Inc. and subsidiary ("Aethlon", the "Company", "we" or "us") is a medical device company focused on creating innovative devices that address unmet medical needs in cancer, infectious disease and other life-threatening conditions. At the core of our developments is the Aethlon ADAPT™ (Adaptive Dialysis-Like Affinity Platform Technology) system, a medical device platform that converges single or multiple affinity drug agents with advanced plasma membrane technology to create therapeutic filtration devices that selectively remove harmful particles from the entire circulatory system without loss of essential blood components. On June 25, 2013, the United States Food and Drug Administration (FDA) approved an Investigational Device Exemption (IDE) that allows us to initiate human feasibility studies of the Aethlon Hemopurifier® in the United States. Under the feasibility study protocol, we will enroll ten end-stage renal disease patients who are infected with the Hepatitis C virus (HCV) to demonstrate the safety of Hemopurifier therapy. Successful completion of this study will allow us the opportunity to initiate pivotal studies that are required for market clearance to treat HCV and other disease conditions in the United States.

Successful outcomes of human trials will also be required by the regulatory agencies of certain foreign countries where we intend to sell this device. Some of our patents may expire before FDA approval or approval in a foreign country, if any, is obtained. However, we believe that certain patent applications and/or other patents issued more recently will help protect the proprietary nature of the Hemopurifier(R) treatment technology.

In October 2013, our subsidiary, Exosome Sciences, Inc. ("ESI"), commenced operations with a focus on advancing exosome-based strategies to diagnose and monitor the progression of cancer, infectious disease and other life-threatening conditions.

Our common stock is quoted on the OTCQB marketplace administered by the OTC Markets Group under the symbol "AEMD."

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with Generally Accepted Accounting Principles in the United States of America (“GAAP”) for interim financial information and with the instructions to Form 10-Q and applicable sections of Regulation S-X. 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 necessary to make the financial statements not misleading have been included. The condensed consolidated balance sheet as of March 31, 2014 was derived from our audited financial statements. Operating results for the six months ended September 30, 2014 are not necessarily indicative of the results that may be expected for the year ending March 31, 2015. For further information, refer to our Annual Report on Form 10-K for the year ended March 31, 2014, which includes audited financial statements and footnotes as of March 31, 2014 and 2013 and for the years then ended.

NOTE 2. LIQUIDITY

The accompanying consolidated financial statements have been prepared assuming that we will continue as a going concern, which contemplates, among other things, the realization of assets and satisfaction of liabilities in the ordinary course of business. We have incurred continuing losses from operations and at September 30, 2014 are in default on certain debt agreements, have negative working capital of approximately \$2,496,000, and have an accumulated deficit of approximately \$79,336,000. These factors, among other matters, raise substantial doubt about our ability to continue as a going concern. A significant amount of additional capital will be necessary to advance the development of our products to the point at which they may become commercially viable. We intend to fund operations, working capital and other cash requirements for the fiscal year ending March 31, 2015 through debt and/or equity financing arrangements as well as through revenues and related cash receipts under our government contracts (see Note 12).

During the six months ended September 30, 2014, we converted a past due convertible note in the amount of \$660,000 and related accrued interest into equity and also restructured and extended a formerly past due convertible note in the amount of \$225,000. We also eliminated the antidilution price protection on all the remaining outstanding notes and warrants which held such price protection. The combination of all of those actions allowed us to reclassify our derivative liability in the amount of \$10,679,067 into equity.

We are currently addressing our liquidity issue by seeking additional investment capital through private placements of common stock and debt and by applying for additional grants issued by government agencies in the United States. We believe that our cash on hand and funds expected to be received from additional private investments will be sufficient to meet our liquidity needs for fiscal 2015. However, no assurance can be given that we will receive any funds in the form of revenues or in connection with capital raising activities in addition to the funds we have already received.

The successful outcome of future contract-based and fundraising activities cannot be determined at this time and there is no assurance that, even if achieved, we will have sufficient funds to execute our intended business plan or generate positive operating results.

The consolidated financial statements do not include any adjustments related to this uncertainty and as to the recoverability and classification of asset carrying amounts or the amount and classification of liabilities that might result should the Company be unable to continue as a going concern.

NOTE 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The summary of our significant accounting policies presented below is designed to assist the reader in understanding our condensed consolidated financial statements. Such financial statements and related notes are the representations of our management, who are 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 majority-owned and controlled subsidiary, ESI. All significant intercompany balances and transactions have been eliminated in consolidation. The Company classifies the noncontrolling interests in ESI as part of consolidated net loss in the six months ended September 30, 2014 and includes the accumulated amount of noncontrolling interests as part of stockholders' equity. During the fiscal year ended March 31, 2014, ESI raised capital in the amount of \$1,500,000 in exchange for the issuance of 300,000 shares of ESI common stock to ESI's investors, representing 20% of ESI's issued and outstanding capital stock. As a result, Aethlon Medical, Inc.'s ownership of ESI was reduced to 80%. If a further change in Aethlon Medical Inc.'s ownership of ESI results in loss of control and deconsolidation, any retained ownership interest will be remeasured with the gain or loss reported in our statement of operations.

The losses at ESI during the six months ended September 30, 2014 reduced the noncontrolling interests on our consolidated balance sheet by \$89,135 from \$218,270 at March 31, 2014 to \$129,135 at September 30, 2014.

USE OF ESTIMATES

We prepare our condensed consolidated financial statements in conformity with GAAP, which requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and reported amounts of revenues and expenses during the reporting periods. Significant estimates made by management include, among others, realization of long-lived assets, estimating fair value associated with debt and equity transactions and valuation of deferred tax assets. Actual results could differ from those estimates.

CASH AND CASH EQUIVALENTS

Accounting standards define "cash and cash equivalents" as any short-term, highly liquid investment that is both readily convertible to known amounts of cash and so near their maturity that they present insignificant risk of changes in value because of changes in interest rates. For the purpose of financial statement presentation, we consider all highly liquid investment instruments with original maturities of three months or less when purchased, or any investment redeemable without penalty or loss of interest to be cash equivalents. As of September 30, 2014 and March 31, 2014, we had no assets that were classified as cash equivalents.

CONCENTRATIONS OF CREDIT RISKS

Cash is maintained at two financial institutions in checking accounts and related cash management accounts. Accounts at these institutions are secured by the Federal Deposit Insurance Corporation ("FDIC") up to \$250,000. Our September 30, 2014 cash balances were approximately \$276,000 over such insured amount. We do not believe that the Company is exposed to any significant risk with respect to its cash.

All of our accounts receivable at September 30, 2014 and March 31, 2014 and all of our revenue in the six month periods ended September 30, 2014 and 2013 were directly from the U.S. Department of Defense or from a subcontract under Battelle (defined herein), which is a prime contractor with the U.S. Department of Defense, and as such no allowance for uncollectable accounts receivable is deemed necessary at September 30, 2014 or March 31, 2014.

FAIR VALUE OF FINANCIAL INSTRUMENTS

The carrying amount of our cash, accounts receivable, accounts payable, and other current liabilities approximate their estimated fair values due to the short-term maturities of those financial instruments. The carrying amount of the notes payable approximates their fair value due to the short maturity of the notes and since the interest rate approximates current market interest rates for similar instruments.

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Management has concluded that it is not practical to determine the estimated fair value of amounts due to related parties because the transactions cannot be assumed to have been consummated at arm's length, the terms are not deemed to be market terms, there are no quoted values available for these instruments, and an independent valuation would not be practicable due to the lack of data regarding similar instruments, if any, and the associated potential costs.

See Note 9 with respect to derivative liabilities.

PROPERTY AND EQUIPMENT

Property and equipment are stated at cost. Depreciation is computed using the straight-line method over the estimated useful lives of the related assets, which range from two to five years. Repairs and maintenance are charged to expense as incurred while improvements are capitalized. Upon the sale or retirement of property and equipment, the accounts are relieved of the cost and the related accumulated depreciation with any gain or loss included in the consolidated statements of operations.

INCOME TAXES

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to the difference between the consolidated financial statements and their respective tax basis. Deferred income taxes reflect the net tax effects of (a) temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts reported for income tax purposes, and (b) tax credit carryforwards. We record a valuation allowance for deferred tax assets when, based on our best estimate of taxable income (if any) in the foreseeable future, it is more likely than not that some portion of the deferred tax assets may not be realized.

IMPAIRMENT OR DISPOSAL OF LONG-LIVED ASSETS

Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that their carrying amounts may not be recoverable. If the cost basis of a long-lived asset is greater than the projected future undiscounted net cash flows from such asset, an impairment loss is recognized. We believe no impairment charges were necessary during the three and six month periods ended September 30, 2014 and 2013.

LOSS PER COMMON SHARE

Basic loss per share is computed by dividing net income available to common stockholders by the weighted average number of common shares outstanding during the period of computation. Diluted loss per share is computed similar to basic loss per share except that the denominator is increased to include the number of additional common shares that would have been outstanding if potential common shares had been issued, if such additional common shares were dilutive. Since we had net losses for all periods presented, basic and diluted loss per share are the same, and additional potential common shares have been excluded as their effect would be antidilutive.

As of September 30, 2014 and 2013, a total of 139,672,815 and 137,935,529 potential common shares, consisting of shares underlying outstanding stock options, warrants and convertible notes payable were excluded as their inclusion would be antidilutive.

SEGMENTS

Historically, we operated in one segment that was based on our development of therapeutic devices. However in the December 2013 quarter, we initiated the operations of ESI to develop diagnostic tests. As a result, we now operate in two segments, Aethlon for therapeutic applications and ESI for diagnostic applications (See Note 14).

DEFERRED FINANCING COSTS

Costs related to the issuance of debt are capitalized and amortized to interest expense over the life of the related debt using the effective interest method. We recorded amortization expense related to our deferred offering costs of \$21,502 and \$863 during the six month periods ended September 30, 2014 and 2013, respectively.

REVENUE RECOGNITION

DARPA Contract -- With respect to revenue recognition, we entered into a government contract with DARPA and have recognized revenue under such contract. We adopted the Milestone method of revenue recognition for the DARPA contract under ASC 605-28 "Revenue Recognition – Milestone Method" and we believe we meet the requirements under ASC 605-28 for reporting contract revenue under the Milestone Method.

In order to account for this contract, we identify the deliverables included within the contract and evaluate which deliverables represent separate units of accounting based on if certain criteria are met, including whether the delivered element has standalone value to the collaborator. The consideration received is allocated among the separate units of accounting, and the applicable revenue recognition criteria are applied to each of the separate units.

A milestone is an event having all of the following characteristics:

(1) There is substantive uncertainty at the date the arrangement is entered into that the event will be achieved. A vendor's assessment that it expects to achieve a milestone does not necessarily mean that there is not substantive uncertainty associated with achieving the milestone.

(2) The event can only be achieved based in whole or in part on either: (a) the vendor's performance; or (b) a specific outcome resulting from the vendor's performance.

(3) If achieved, the event would result in additional payments being due to the vendor.

A milestone does not include events for which the occurrence is either: (a) contingent solely upon the passage of time; or (b) the result of a counterparty's performance.

The policy for recognizing deliverable consideration contingent upon achievement of a milestone must be applied consistently to similar deliverables.

The assessment of whether a milestone is substantive is performed at the inception of the arrangement. The consideration earned from the achievement of a milestone must meet all of the following for the milestone to be considered substantive:

(1) The consideration is commensurate with either: (a) the vendor's performance to achieve the milestone; or (b) the enhancement of the value of the delivered item or items as a result of a specific outcome resulting from the vendor's performance to achieve the milestone;

(2) The consideration relates solely to past performance; and

(3) The consideration is reasonable relative to all of the deliverables and payment terms (including other potential milestone consideration) within the arrangement.

A milestone is not considered substantive if any portion of the associated milestone consideration relates to the remaining deliverables in the unit of accounting (i.e., it does not relate solely to past performance). To recognize the milestone consideration in its entirety as revenue in the period in which the milestone is achieved, the milestone must be substantive in its entirety. Milestone consideration cannot be bifurcated into substantive and non-substantive components. In addition, if a portion of the consideration earned from achieving a milestone may be refunded or adjusted based on future performance, the related milestone is not considered substantive.

See Note 12 for the additional disclosure information required under ASC 605-28.

Battelle Subcontract -- We entered into a subcontract agreement with Battelle Memorial Institute ("Battelle") in March 2013. Battelle was chosen by DARPA to be the prime contractor on the systems integration portion of the original DARPA contract and we are one of several subcontractors on that systems integration project. The Battelle subcontract is cost-reimbursable under a time and materials basis. We began generating revenues under the subcontract during the six months ended September 30, 2013.

Our revenue under this contract is a function of cost reimbursement plus an overhead mark-up for hours devoted to the project by specific employees (with specific hourly rates for those employees). Battelle engages us as needed. Each payment requires approval by the program manager at Battelle.

STOCK-BASED COMPENSATION

Employee stock options and rights to purchase shares under stock participation plans are accounted for under the fair value method. Accordingly, share-based compensation is measured when all granting activities have been completed, generally the grant date, based on the fair value of the award. The exercise price of options is generally equal to the market price of the Company's common stock (defined as the closing price as quoted on the OTCBB on the date of grant). Compensation cost recognized by the Company includes (a) compensation cost for all equity incentive awards granted prior to April 1, 2006, but not yet vested, based on the grant-date fair value estimated in accordance with the original provisions of the then current accounting standards, and (b) compensation cost for all equity incentive awards granted subsequent to April 1, 2006, based on the grant-date fair value estimated in accordance with the provisions of subsequent accounting standards. We use a Binomial Lattice option pricing model for estimating fair value of options granted (see Note 10).

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The following table summarizes share-based compensation expenses relating to shares and options granted and the effect on loss per common share during the six month periods ended September 30, 2014 and 2013:

	Six Months Ended September 30, 2014	Six Months Ended September 30, 2013
Vesting of Stock Options	\$260,680	\$124,243
Incremental fair value of option Modifications	–	1,914
Vesting Expense Associated with CEO Restricted Stock Grant	–	64,444
Total Stock-Based Compensation Expense	\$260,680	\$190,601
Weighted average number of common shares outstanding – basic and diluted	243,494,916	182,004,220
Basic and diluted loss per common share	\$(0.00) \$(0.00

We account for transactions involving services provided by third parties where we issue equity instruments as part of the total consideration using the fair value of the consideration received (i.e. the value of the goods or services) or the fair value of the equity instruments issued, whichever is more reliably measurable. In transactions, when the value of the goods and/or services are not readily determinable and (1) the fair value of the equity instruments is more reliably measurable and (2) the counterparty receives equity instruments in full or partial settlement of the transactions, we use the following methodology:

- For transactions where goods have already been delivered or services rendered, the equity instruments are issued on or about the date the performance is complete (and valued on the date of issuance).
- For transactions where the instruments are issued on a fully vested, non-forfeitable basis, the equity instruments are valued on or about the date of the contract.
- For any transactions not meeting the criteria in (a) or (b) above, we re-measure the consideration at each reporting date based on its then current stock value.

We review share-based compensation on a quarterly basis for changes to the estimate of expected award forfeitures based on actual forfeiture experience. The effect of adjusting the forfeiture rate for all expense amortization after March 31, 2006 is recognized in the period the forfeiture estimate is changed. The effect of forfeiture adjustments for the six months ended September 30, 2014 was insignificant.

PATENTS

Patents include both foreign and domestic patents. There were several patents pending at September 30, 2014. We capitalize the cost of patents and patents pending, some of which were acquired, and amortize such costs over the shorter of the remaining legal life or their estimated economic life, upon issuance of the patent. The unamortized costs of patents and patents pending are subject to our review for impairment under our long-lived asset policy above.

STOCK PURCHASE WARRANTS

We grant warrants in connection with the issuance of convertible notes payable and the issuance of common stock for cash. When such warrants are classified as equity and issued in connection with debt, we measure the relative estimated fair value of such warrants and record it as a discount from the face amount of the convertible notes payable. Such discounts are amortized to interest expense over the term of the notes using the effective interest method. Warrants issued in connection with common stock for cash, if classified as equity, are considered issued in connection with equity transactions and the warrant fair value is recorded to additional paid-in-capital. Lastly, warrants not meeting equity classification are recorded as derivative instruments.

DERIVATIVE INSTRUMENTS

We evaluate free-standing derivative instruments (or embedded derivatives) to properly classify such instruments within equity or as liabilities in our financial statements. Our policy is to settle instruments indexed to our common shares on a first-in-first-out basis.

The classification of a derivative instrument is reassessed at each reporting date. If the classification changes as a result of events during a reporting period, the instrument is reclassified as of the date of the event that caused the reclassification. There is no limit on the number of times a contract may be reclassified.

Instruments classified as derivative liabilities are remeasured each reporting period (or upon reclassification) and the change in fair value is recorded on our consolidated statement of operations in other (income) expense.

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BENEFICIAL CONVERSION FEATURE OF CONVERTIBLE NOTES PAYABLE

The convertible feature of certain notes payable provides for a rate of conversion that is below market value. Such feature is normally characterized as a "Beneficial Conversion Feature" ("BCF"). We measure the estimated fair value of the BCF in circumstances in which the conversion feature is not required to be separated from the host instrument and accounted for separately, and record that value in the consolidated financial statements as a discount from the face amount of the notes. Such discounts are amortized to interest expense over the term of the notes.

REGISTRATION PAYMENT ARRANGEMENTS

We account for contingent obligations to make future payments or otherwise transfer consideration under a registration payment arrangement separately from any related financing transaction agreements, and any such contingent obligations are recognized only when it is determined that it is probable we will become obligated for future payments and the amount, or range of amounts, of such future payments can be reasonably estimated.

RESEARCH AND DEVELOPMENT EXPENSES

We incurred research and development expenses during the three and six month periods ended September 30, 2014 and 2013, which are included in various operating expense line items in the accompanying condensed consolidated statements of operations. Our research and development expenses in those periods were as follows:

	September 30, 2014	September 30, 2013
Three months ended	\$ 250,388	\$ 293,580
Six months ended	\$ 637,723	\$ 626,638

OFF-BALANCE SHEET ARRANGEMENTS

We have not entered into any off-balance sheet arrangements that have or are reasonably likely to have a current or future material effect on our consolidated financial statements.

SIGNIFICANT RECENT ACCOUNTING PRONOUNCEMENTS

Management is evaluating significant recent accounting pronouncements that are not yet effective for the Company, including the new accounting standard on revenue recognition, ASU 2014-09 (Topic 606), and has not yet concluded whether any such pronouncements will have a significant effect on the Company's future consolidated financial statements.

NOTE 4. NOTES PAYABLE

Notes payable consist of the following:

	September 30, 2014		March 31, 2014	
	Principal Balance	Accrued Interest	Principal Balance	Accrued Interest
12% Notes payable, past due	\$ 185,000	\$ 367,687	\$ 185,000	\$ 353,813
10% Note payable, past due	5,000	6,625	5,000	6,375
Directors' Note(s)	–	–	200,000	14,516
Total	\$ 190,000	\$ 374,312	\$ 390,000	\$ 374,704

During the six months ended September 30, 2014, we recorded interest expense of \$19,959 related to the contractual interest rates of our notes payable.

12% NOTES

From August 1999 through May 2005, we entered into various borrowing arrangements for the issuance of notes payable from private placement offerings (the "12% Notes"). On April 21, 2010, a holder of \$100,000 of the 12% Notes converted the principal balance and \$71,758 of accrued interest into 687,033 shares of common stock at an agreed conversion price of \$0.25 per share. At September 30, 2014, the 12% Notes in the principal amount of \$185,000 were past due, in default, and bearing interest at the default rate of 15%.

10% NOTES

At September 30, 2014, one 10% Note in the amount of \$5,000 is past due and in default, remains outstanding and bears interest at the default rate of 15%.

Management's plans to satisfy the remaining outstanding balance on these 12% and 10% Notes include converting the notes to common stock at market value or repayment when funds are available.

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DIRECTORS' NOTES

In July 2013, we borrowed \$400,000 from two of our directors under two 90 day notes for \$200,000 each bearing 10% interest (the "Notes"). At the discretion of the holders, if not paid off by October 9, 2013, the noteholders were entitled to (i) convert the principal and accrued interest under the Notes into shares of common stock at \$0.088 per share (the "Conversion Price") and (ii) receive warrants to purchase common stock equal to 50% of the principal converted under the Notes, with an exercise price of \$0.132 per share. Additionally, there was a provision for a penalty interest rate of 12%.

That potential conversion price and warrant exercise price were based on the same pricing mechanism that we have used in prior equity unit financings since March 2012 (see Note 6) which are based on 80% of the then current market price of our common stock and with the warrant exercise price based on 120% of the same then current market price. We initially reserved 6,931,818 shares of common stock to support the conversion of the Notes and accrued interest in full as well as the exercise of the warrants in full (should such conversion and/or issuance occur).

During the fiscal year ended March 31, 2014, the principal of \$200,000 and accrued interest of \$9,367 were paid on one of the Notes, which extinguished all potential common stock and warrant issuance provisions related to that Note.

During the six months ended September 30, 2014, the holder of the second Note converted the principal of \$200,000 and accrued interest of \$20,349 into 2,503,966 shares of our common stock per the conversion formula of the Note (see Note 6).

5. CONVERTIBLE NOTES PAYABLE

Convertible Notes Payable consisted of the following at September 30, 2014:

	Principal	Unamortized Discount	Net Amount	Accrued Interest
Convertible Notes Payable – Current Portion:				
October & November 2009 10% Convertible Notes	\$ 50,000	\$ –	\$ 50,000	\$ 28,598
April 2010 10% Convertible Note	75,000	–	75,000	35,188
July and August 2011 10% Convertible Notes, past due	283,421	–	283,421	96,728
Law Firm Note	75,000	–	75,000	9,479
Total – Convertible Notes Payable – Current Portion	483,422	–	483,422	169,993

Explanation of Responses:

Convertible Notes Payable – Non-Current Portion:

Amended and Restated Series A 12% Convertible Notes	225,000	–	225,000	9,000
September 2010 12% Convertible Notes	317,072	–	317,072	9,513
April 2011 12% Convertible Notes	448,448	–	448,448	13,454
Total – Convertible Notes Payable – Non-Current Portion	990,520	–	990,520	31,967
Total Convertible Notes Payable	\$1,473,941	\$	–	\$1,473,941 \$201,960

There were no discounts remaining on any of our Convertible Notes Payable as of September 30, 2014.

During the six months ended September 30, 2014, we recorded interest expense of \$97,362 related to the contractual interest rates of our convertible notes and interest expense of \$21,502 related to the amortization of deferred financing costs related to the convertible notes for a total interest related to convertible notes of \$118,864.

Convertible Notes Payable consisted of the following at March 31, 2014:

	Principal	Unamortized Discount	Net Amount	Accrued Interest
Convertible Notes Payable – Current Portion:				
Amended and Restated Series A 12% Convertible Notes, past due	\$885,000	\$ –	\$885,000	\$575,250
2008 10% Convertible Notes, past due	25,000	–	25,000	19,167
October & November 2009 10% Convertible Notes	50,000	–	50,000	26,097
April 2010 10% Convertible Note	75,000	–	75,000	31,438
July and August 2011 10% Convertible Notes, past due	257,655	–	257,655	90,256
Law Firm Note	75,000	–	75,000	7,604
Total – Convertible Notes Payable – Current Portion	1,367,655	–	1,367,655	749,812
Convertible Notes Payable – Non-Current Portion:				
September 2010 12% Convertible Notes	317,072	–	317,072	35,034
April 2011 12% Convertible Notes	448,448	–	448,448	12,117
September 2011 12% Convertible Notes	10,931	–	10,931	–
Total – Convertible Notes Payable – Non-Current Portion	776,451	–	776,451	47,151
Total Convertible Notes Payable	\$2,144,106	\$ –	\$2,144,106	\$796,963

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There were no discounts remaining on any of our Convertible Notes Payable as of March 31, 2014.

AMENDED AND RESTATED SERIES A 12% CONVERTIBLE NOTES

In June 2010, we entered into Amended and Restated Series A 12% Convertible Promissory Notes (the "Amended and Restated Notes") with the holders of certain promissory notes previously issued by us, extending the due date to December 31, 2010 on the aggregate principal balance of \$900,000. During the fiscal year ended March 31, 2013, the holders of \$15,000 of the Notes converted their principal and related accrued interest into common stock. The balance remaining at March 31, 2014 was \$885,000 and past due.

Weiner Note Conversion

On June 24, 2014, we entered into an agreement with the Ellen R. Weiner Family Revocable Trust (the "Trust"), a holder of a Series A 12% Convertible Note (the "Note"), which previously was classified as being in default. As per the agreement, the Trust converted past due principal of \$660,000 and accrued interest balance of \$343,200 into restricted common stock.

Additionally, the Trust agreed to waive anti-dilution price protection underlying warrants previously issued to the Trust. On June 26, 2014, three other parties who held similar warrants also agreed to waive their anti-dilution price protection.

Under its agreement, the Trust converted the entire \$1,003,200 past due principal and interest balance on the Note, which previously was in default, into an aggregate of 23,318,254 restricted shares of our common stock and five-year warrants to acquire up to 6,809,524 shares of our common stock at an exercise price of \$.042 per share (which exercise price was the result of certain contractual price adjustments previously made during 2011) and up to 397,222 shares of our common stock at an exercise price of \$.108 per share (collectively, the "Conversion Securities"). Based on the fair value of the warrants and shares issued to the Trust for the accrued interest, we recorded a loss on settlement of notes of \$1,791,421.

In exchange for the Trust's conversion in full of the Note and accrued interest and for the waivers of anti-dilution price protection in the previously issued warrants, in addition to the Conversion Securities, we issued to the Trust 75,000 restricted shares of common stock as a service fee, changed the exercise price of all of the previously issued warrants to \$.042 per share and extended the expiration date of all of the previously issued warrants to July 1, 2018. We valued the 75,000 share service fee at \$12,000 based on our closing price on the date of the agreement and recorded that

value as interest expense during the June 2014 period.

Bird Estate Extension

On July 8, 2014, we executed a written restructuring agreement (the “Agreement”) with the Estate of Allan Bird (the “Estate”), a holder of a Series A 12% Convertible Note (the “Note”), which previously was classified as being in default. Since the negotiations for the Agreement were completed in the month of June, we recorded the impact of the Agreement as of June 30, 2014. In the Agreement, the Estate agreed to extend the expiration date of the Note to April 1, 2016, to convert approximately \$116,970 of accrued interest to equity, and to waive anti-dilution price protection underlying the Note and warrants previously issued to the Estate.

Under the Agreement, the Estate converted the entire \$116,970 past due interest balance on the Note, which previously was in default, into an aggregate of 2,591,846 restricted shares of our common stock. The Estate received five-year warrants to acquire up to 2,321,429 shares of our common stock at an exercise price of \$.042 per share (which exercise price was the result of certain contractual price adjustments previously made during 2011). Based on our common stock prices during a period of negotiation with the Estate including during calendar year 2013, the Estate also received five-year warrants to acquire up to 135,417 shares of our common stock at an exercise price of \$.108 (collectively known as the “Conversion Securities”). Based on the fair value of the warrants and shares issued to the Estate for the accrued interest, we recorded a loss on settlement of notes of \$663,209.

In exchange for the Estate’s extension of the Note, conversion of accrued interest and for the waivers of anti-dilution price protection in the previously issued warrants, in addition to the Conversion Securities, we also issued to the Estate 25,000 restricted shares of common stock as an extension fee and extended the expiration date of all of the previously issued warrants to July 1, 2018. We valued the 25,000 share extension fee at \$4,500 based on our closing price and recorded that value as a deferred financing cost, which we will amortize over the extended two year life of the note.

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2008 10% CONVERTIBLE NOTES

On September 17, 2014, we issued to the holder of the remaining 2008 10% Convertible Note units consisting of an aggregate of 478,188 shares of restricted common stock and unit warrants to acquire up to an aggregate of 239,094 shares of common stock at an exercise price of \$0.096 per share (see Note 6). The units were issued to the Note holder upon the conversion of an aggregate of \$45,906 of unpaid principal and accrued interest due under the Note, which represented the entire amount outstanding under the Note and the Note was retired. We recorded a loss on debt conversion of \$65,493 on this transaction.

OCTOBER & NOVEMBER 2009 10% CONVERTIBLE NOTES

In October and November 2009, we raised \$430,000 from the sale to accredited investors of 10% convertible notes ("October & November 2009 10% Convertible Notes"). The October & November 2009 10% Convertible Notes matured at various dates between April 2011 and May 2011 and are convertible into our common stock at a fixed conversion price of \$0.25 per share. The investors also received matching three year warrants to purchase unregistered shares of our common stock at an exercise price of \$0.25 per share. We measured the fair value of the warrants and the beneficial conversion feature of the Notes and recorded a 100% discount against the principal of the notes. Such discount was fully amortized at March 31, 2014.

In July 2012, we issued 461,409 shares of common stock and 230,705 warrants to purchase common stock to the holder of a \$25,000 note in this grouping in exchange for the conversion of such note and related accrued interest of \$8,000 (for a total of \$33,000). The warrants expired in 2012 and are exercisable at \$0.107 per share (see Note 6). We recorded a loss on conversion of \$45,796.

The following table shows the conversions into principal of the October and November 2009 10% Convertible Notes by fiscal year:

Activity in October & November 2009 10% Convertible Notes	
Initial principal balance	\$450,250
Conversions during the fiscal year ended March 31, 2010	(70,000)
Conversions during the fiscal year ended March 31, 2011	(175,000)
Conversions during the fiscal year ended March 31, 2012	(130,250)
Conversions during the fiscal year ended March 31, 2013	(25,000)
Conversions during the fiscal year ended March 31, 2014	–
Conversions during the six months ended September 30, 2014	–
Balance as of September 30, 2014	\$50,000

Explanation of Responses:

On March 31, 2012, we agreed to extend the expiration date and to change the exercise price of certain warrants of one of the note holders by two years in exchange for the extension of \$50,000 of the October & November 2009 10% Convertible Notes and the \$75,000 April 2010 10% Convertible Note (see below) by that same two year period. We recorded a charge of \$77,265 relating to this modification.

In September 2013, we agreed to extend the expiration date of certain warrants of one of the note holders by two years in exchange for the extension of \$50,000 of the October & November 2009 10% Convertible Notes and the \$75,000 April 2010 10% Convertible Note (see below) by that same two year period. Management assessed the change in the value of the notes and related warrants before and after that extension and determined that the change in value related to the change in terms was not significant.

Subsequent to September 30, 2014, we issued to the holder of the remaining October & November 2009 10% Convertible Note and the April 2010 10% Convertible Note units consisting of an aggregate of 1,835,798 shares of common stock and unit warrants to acquire up to an aggregate of 1,837,798 shares of common stock at an exercise price of \$0.103 per share. The units were issued to the note holder upon the conversion of an aggregate of \$189,087 of unpaid principal and accrued interest due under two promissory notes (the remaining October & November 2009 10% Convertible Note and the April 2010 10% Convertible Note). The amounts converted represented the entire principal and interest outstanding under the notes and the notes held by that holder were retired (see Note 15).

APRIL 2010 10% CONVERTIBLE NOTE

In April 2010, we raised \$75,000 from the sale to an accredited investor of a 10% convertible note. The convertible note was originally scheduled to mature in October 2011 and is convertible into our common stock at a fixed conversion price of \$0.25 per share prior to maturity. The investor also received three year warrants to purchase 300,000 unregistered shares of our common stock at a price of \$0.25 per share.

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We measured the fair value of the warrants and the beneficial conversion feature of the notes and recorded a 100% discount against the principal of the notes. We amortized this discount using the effective interest method over the term of the note. As of September 30, 2014, there have not been any conversions of the April 2010 10% Convertible Note.

On March 31, 2012, we agreed to extend the expiration date and to change the exercise price of certain warrants of the note holder by two years in exchange for his extension of \$50,000 of the October & November 2009 10% Convertible Notes and the \$75,000 April 2010 10% Convertible Note by that same two year period.

In September 2013, we agreed to extend the expiration date of certain warrants of one of the note holders by two years in exchange for the extension of \$50,000 of the October & November 2009 10% Convertible Notes and the \$75,000 April 2010 10% Convertible Note (see below) by that same two year period. Management assessed the change in the value of the notes and related warrants before and after that extension and determined that the change in value related to the change in terms was not significant.

Subsequent to September 30, 2014, we issued to the holder of the remaining October & November 2009 10% Convertible Note and the April 2010 10% Convertible Note units consisting of an aggregate of 1,835,798 shares of common stock and unit warrants to acquire up to an aggregate of 1,837,798 shares of common stock at an exercise price of \$0.103 per share. The units were issued to the note holder upon the conversion of an aggregate of \$189,087 of unpaid principal and accrued interest due under two promissory notes (the remaining October & November 2009 10% Convertible Note and the April 2010 10% Convertible Note). The amounts converted represented the entire principal and interest outstanding under the notes and the notes held by that holder were retired (see Note 15).

SEPTEMBER 2010 10% CONVERTIBLE NOTES

On September 3, 2010, we entered into a Subscription Agreement with three accredited investors (the "Purchasers") providing for the issuance and sale of convertible promissory notes and corresponding warrants in the aggregate principal amount of \$1,430,000. The initial closing under the Subscription Agreement resulted in the issuance and sale of (i) convertible promissory notes in the aggregate principal amount of \$743,600, (ii) five-year warrants to purchase an aggregate of 3,718,000 shares of our common stock at an exercise price of \$0.31125 per share, and (iii) five-year warrants to purchase an aggregate of 3,718,000 shares of our common stock at an exercise price of \$0.43575 per share. The convertible promissory notes bear interest compounded monthly at the annual rate of ten percent (10%) and mature on April 1, 2016 (see below). The aggregate gross cash proceeds were \$650,000, the balance of the principal amount representing a due diligence fee and an original issuance discount. The convertible promissory notes are convertible at the option of the holders into shares of our common stock at a price per share equal to eighty percent (80%) of the average of the three lowest closing bid prices of the common stock as reported by Bloomberg L.P. for the principal market on which the common stock trades or is quoted for the ten (10) trading days preceding the proposed conversion date. Subject to adjustment as described in the notes, the conversion price may not

be more than \$0.30 nor less than \$0.20. There are no registration requirements with respect to the shares of common stock underlying the notes or the warrants.

On March 31, 2014, we entered into separate Amendments to Convertible Notes and Warrants (collectively, the "Amendments") with three accredited investors (collectively, the "Investors") who own certain convertible promissory notes (collectively, the "Notes") and warrants (collectively, the "Warrants") previously issued by us on various dates between December 5, 2007 and September 23, 2011, including the September 2010 Convertible Notes.

Prior to the Amendments, the Notes were past maturity and were in default, resulting in the accrual of interest at the applicable default interest rate. The Amendments extended the maturity date of each of the Notes to April 1, 2016, which permits us to classify them as long-term liabilities. As a result of the Amendments, the Notes are no longer in default and the non-default interest rate for all of the Notes was set at 12% per annum, which represents a reduction from the default interest rates of fifteen percent at which interest had been accruing. By entering into the Amendments, we also agreed to increase the currently outstanding principal amount of the Notes by 12% from a total of \$693,260 to a total of \$776,451.

During the period from October 2011 to February 2014, the Investors had converted, at conversion prices between \$.0546 and \$.07 per share, portions of principal and interest outstanding under the Notes and certain other convertible promissory notes previously issued to them by us. Certain antidilution provisions applicable to such notes should have resulted in such conversions being effected at a conversion price of \$.042 per share. Accordingly, pursuant to the Amendments, we issued to the investors an aggregate of 4,507,105 shares of the Company's Common Stock, which represents the additional shares of Common Stock that would have been issued to the Investors had such conversions been effected at \$.042 per share.

The Amendments also set the conversion price of the Notes, as well as the exercise price at which shares of our common stock can be purchased under the Warrants, at \$.042 per share. By virtue of the Amendments, the expiration dates of the Warrants also were extended from dates between September 3, 2015 and September 23, 2016 to January 1, 2017.

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The following table shows the activity in the September 2010 10% Convertible Notes by fiscal year:

Activity in the September 2010 10% Convertible Notes	
Initial principal balance	\$743,600
Conversions during the fiscal year ended March 31, 2012	(405,500)
Conversions during the fiscal year ended March 31, 2013	(30,000)
Conversions during the fiscal year ended March 31, 2014	(25,000)
Increase in principal balance due to 12% extension fee	33,972
Conversions during the six months ended September 30, 2014	–
Balance as of September 30, 2014	\$317,072

APRIL 2011 10% CONVERTIBLE NOTES

In April 2011, we entered into a Subscription Agreement with two accredited investors (the “Purchasers”) providing for the issuance and sale of convertible promissory notes and corresponding warrants in the aggregate principal amount of \$385,000. The closing under the Subscription Agreement resulted in the issuance and sale by us of (i) convertible promissory notes in the aggregate principal amount of \$385,000, (ii) five-year warrants to purchase an aggregate of 4,004,000 shares of our common stock at an exercise price of \$0.125 per share, and (iii) five-year warrants to purchase an aggregate of 4,004,000 shares of our common stock at an exercise price of \$0.175 per share. The convertible promissory notes bear interest compounded monthly at the annual rate of 10% and mature on April 1, 2016 (see below). The aggregate gross cash proceeds to us were \$350,000, the balance of the principal amount representing a due diligence fee and an original issuance discount. The convertible promissory notes are convertible at the option of the holders into shares of our common stock at a price per share equal to eighty percent (80%) of the average of the three lowest closing bid prices of the common stock as reported by Bloomberg L.P. for the principal market on which the common stock trades or is quoted for the ten (10) trading days preceding the proposed conversion date. Subject to adjustment as described in the notes, the conversion price may not be more than \$0.20 nor less than \$0.10. There are no registration requirements with respect to the shares of common stock underlying the notes or the warrants.

In addition, we issued (i) five-year warrants to purchase an aggregate of 812,500 shares of our common stock at an exercise price of \$0.125 per share, and (ii) five-year warrants to purchase an aggregate of 812,500 shares of our common stock at an exercise price of \$0.175 per share to the Purchasers. These warrants were issued as an antidilution adjustment under certain common stock purchase warrants held by the Purchasers that were acquired from us in September 2010.

On March 31, 2014, we entered into separate Amendments to Convertible Notes and Warrants (collectively, the “Amendments”) with three accredited investors (collectively, the “Investors”) who own certain convertible promissory notes (collectively, the “Notes”) and warrants (collectively, the “Warrants”) previously issued by us on various dates between December 5, 2007 and September 23, 2011, including the April 2011 Convertible Notes.

Prior to the Amendments, the Notes were past maturity and were in default, resulting in the accrual of interest at the applicable default interest rate. The Amendments extended the maturity date of each of the Notes to April 1, 2016, which permits us to classify them as long-term liabilities. As a result of the Amendments, the Notes are no longer in default and the non-default interest rate for all of the Notes was set at 12% per annum, which represents a reduction from the default interest rates of 15% at which interest had been accruing. By entering into the Amendments, we also agreed to increase the currently outstanding principal amount of the Notes by 12% from a total of \$693,260 to a total of \$776,451.

During the period from October 2011 to February 2014, the Investors had converted, at conversion prices between \$.0546 and \$.07 per share, portions of principal and interest outstanding under the Notes and certain other convertible promissory notes previously issued to them by us. Certain antidilution provisions applicable to such notes should have resulted in such conversions being effected at a conversion price of \$.042 per share. Accordingly, pursuant to the Amendments, we issued to the investors an aggregate of 4,507,105 shares of the Company's Common Stock, which represents the additional shares of Common Stock that would have been issued to the Investors had such conversions been effected at \$.042 per share.

The Amendments also set the conversion price of the Notes, as well as the exercise price at which shares of our common stock can be purchased under the Warrants, at \$.042 per share. By virtue of the Amendments, the expiration dates of the Warrants also were extended from dates between September 3, 2015 and September 23, 2016 to January 1, 2017.

As of September 30, 2014, there have not been any conversions of the April 2011 10% Convertible Notes and the 12% extension fee noted above increased the principal balance by \$48,048 to a principal balance of \$448,448.

JULY & AUGUST 2011 10% CONVERTIBLE NOTES

During the three months ended September 30, 2011, we raised \$357,656 in five separate 10% convertible notes. Those notes had a fixed conversion price of \$0.09 per share and carried an interest rate of 10%. The convertible notes matured in July and August 2012. We also issued those investors five year warrants to purchase 3,973,957 shares of common stock at \$0.125 per share.

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We measured the fair value of the warrants and the beneficial conversion feature of the notes and recorded a \$257,926 discount against the principal of the notes. We amortized this discount using the effective interest method over the term of the note.

Effective March 31, 2014, the holders of three of the five notes totaling \$100,000 converted all of their principal and accrued interest into 1,438,700 shares of our common stock at the contractual conversion price of \$0.09 per share.

In September 2014, we entered into a forbearance agreement with the holder of the remaining two notes in which we agreed to repay his notes by October 31, 2014 and in which we also agreed to extend his warrants by two years. We recorded a charge of \$143,363 in the September 2014 period related to this warrant extension due to the change in the fair value of the warrants.

Subsequent to September 30, 2014, we paid off in full the remaining outstanding principal balance and interest balances on the two remaining notes with cash payments of \$382,748 (see Note 15).

SEPTEMBER 2011 CONVERTIBLE NOTES

In September 2011, we issued \$253,760 of convertible notes, convertible at \$0.07 per share. Such notes originally matured in September 2012.

On March 31, 2014, we entered into separate Amendments to Convertible Notes and Warrants (collectively, the "Amendments") with three accredited investors (collectively, the "Investors") who own certain convertible promissory notes (collectively, the "Notes") and warrants (collectively, the "Warrants") previously issued by us on various dates between December 5, 2007 and September 23, 2011, including the September 2011 Convertible Notes.

Prior to the Amendments, the Notes were past maturity and were in default, resulting in the accrual of interest at the applicable default interest rate. The Amendments extended the maturity date of each of the Notes to April 1, 2016, which permits us to classify them as long-term liabilities. As a result of the Amendments, the Notes are no longer in default and the non-default interest rate for all of the Notes was set at 12% per annum, which represents a reduction from the default interest rates of 15% at which interest had been accruing. By entering into the Amendments, we also agreed to increase the currently outstanding principal amount of the Notes by 12%, which in the case of the September 2011 Notes, they increased from \$9,760 to \$10,931

During the period from October 2011 to February 2014, the Investors had converted, at conversion prices between \$.0546 and \$.07 per share, portions of principal and interest outstanding under the Notes and certain other convertible promissory notes previously issued to them by us. Certain antidilution provisions applicable to such notes should have resulted in such conversions being effected at a conversion price of \$.042 per share. Accordingly, pursuant to the Amendments, we issued to the investors an aggregate of 4,507,105 shares of the Company's Common Stock, which represents the additional shares of Common Stock that would have been issued to the Investors had such conversions been effected at \$.042 per share.

The Amendments also set the conversion price of the Notes, as well as the exercise price at which shares of our common stock can be purchased under the Warrants, at \$.042 per share. By virtue of the Amendments, the expiration dates of the Warrants also were extended to January 1, 2017.

The following table shows the conversions into principal of the September 2011 Convertible Notes by fiscal year:

Activity in the September 2011 Convertible Notes	
Initial principal balance	\$253,760
Conversions during the fiscal year ended March 31, 2012	(15,000)
Conversions during the fiscal year ended March 31, 2013	(60,000)
Conversions during the fiscal year ended March 31, 2014	(169,000)
Increase in principal balance due to extension fee	1,171
Conversions during the six months ended September 30, 2014	(10,931)
Balance as of September 30, 2014	\$-

As noted in the above table, the remaining balance of the September 2011 Convertible Notes converted into equity during the six months ended September 30, 2014.

LAW FIRM NOTE

On March 22, 2012, we entered into a Promissory Note with our corporate law firm for the amount of \$75,000, which represented the majority of the amount we owed to that firm at that time. The Promissory Note originally had a maturity date of December 31, 2012 and bears interest at 5% per annum. The note is convertible at the option of the holder into shares of our common stock at a 10% discount to the market price of the common stock on the date prior to conversion with a floor price on such conversions of \$0.08 per share. The holder subsequently agreed to extend the Maturity Date of the Note first to October 1, 2013, then to September 30, 2013, and now the expiration date of this note is again extended to October 1, 2014. As of September 30, 2014, there have not been any conversions of the Law Firm Note.

Subsequent to September 30, 2014, we paid off in full the outstanding principal balance and interest balance on the note with a cash payment of \$50,000 and an issuance of 170,020 common shares (see Note 15).

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6. EQUITY TRANSACTIONS

COMMON STOCK AND WARRANTS

The following are Aethlon Medical, Inc.'s Equity Transactions in the Six Months Ended September 30, 2014.

In the three months ended June 30, 2014, we completed unit subscription agreements with seven accredited investors pursuant to which we issued 2,192,444 shares of our common stock and 1,096,222 warrants to purchase our common stock for net cash proceeds of \$320,800. Such warrants have exercise prices ranging from \$0.193 to \$0.236 per share.

As discussed above in Note 5, during the three months ended June 30, 2014, we issued 15,714,286 shares of restricted common stock to the holder of one of the Series A 12% Convertible Notes in exchange for the conversion in full of the \$660,000 principal balance of that note, 7,603,968 shares of restricted common stock in exchange for conversion of \$343,200 of accrued interest and 75,000 shares of restricted common stock as a restructuring fee. During that period, we also issued the other holder of the Series A 12% Convertible Notes 2,591,846 shares of restricted common stock in exchange for conversion of \$116,970 of accrued interest and 25,000 shares of restricted common stock as a restructuring fee.

During the three months ended June 30, 2014, we issued 219,127 shares of common stock pursuant to our S-8 registration statement covering our Amended 2010 Stock Plan at an average price of \$0.17 per share in payment for legal services, internal controls consulting services and regulatory consulting services collectively valued at \$38,268 based on the value of the services provided.

During the three months ended September 30, 2014, we issued 359,956 shares of common stock pursuant to our S-8 registration statement covering our Amended 2010 Stock Plan at an average price of \$0.14 per share in payment for legal and scientific consulting services valued at \$49,090 based on the value of the services provided.

During the three months ended September 30, 2014, we issued 390,301 shares of restricted common stock at an average price of \$0.19 per share in payment for investor relations consulting services valued at \$75,000 based on the value of the services provided.

During the three months ended September 30, 2014, we issued 1,937,505 shares of restricted common stock to the holders of three convertible notes in exchange for the partial or full conversion of principal and interest in the aggregate amount of \$81,375 at a conversion price of \$0.042 per share.

On July 24, 2014, we issued an aggregate of 2,503,966 shares of restricted common stock and a seven-year warrant to issue up to 1,251,983 shares of common stock at an exercise price of \$0.132 per share to Dr. Chetan Shah, a director. The common stock and warrant were issued to Dr. Shah upon the conversion of an aggregate of \$220,349 of unpaid principal and accrued interest due under a 10% Convertible Note previously issued to Dr. Shah by us on July 9, 2013.

On September 17, 2014, we issued to the holder of the remaining 2008 10% Convertible Note units consisting of an aggregate of 478,188 shares of restricted common stock and unit warrants to acquire up to an aggregate of 239,094 shares of common stock at an exercise price of \$0.096 per share (see Note 5). The units were issued to the note holder upon the conversion of an aggregate of \$45,906 of unpaid principal and accrued interest due under the promissory note, which represented the entire amount outstanding under the note. We recorded a loss on debt conversion of \$65,493 on this transaction.

During the three months ended September 30, 2014, we issued to four investors 2,673,231 shares of restricted common stock through the cash exercise of eight warrants for \$259,474 of cash at an average exercise price of approximately \$0.10 per share. As an inducement to those investors, we issued them replacement warrants to acquire up to an aggregate of 2,673,231 shares of common stock on the same terms as the warrants they exercised.

During the three months ended September 30, 2014, we issued and sold to three accredited investors units consisting of (a) one hundred thousand (100,000) restricted shares of our common stock, par value \$.001 per share, at prices per share ranging from \$0.091 to \$0.094 and (b) a five-year warrant to purchase fifty thousand (50,000) shares of common stock at exercise prices ranging from \$0.136 to \$0.143 per share. In total, the investors purchased for cash an aggregate of \$90,000 of units. The investors acquired an aggregate of 974,982 shares of common stock and warrants to acquire up to an aggregate of 487,491 shares of Common Stock.

7. RELATED PARTY TRANSACTIONS

DUE TO RELATED PARTIES

Certain of our officers and other related parties have advanced us funds, agreed to defer compensation and/or paid expenses on our behalf to cover working capital deficiencies. These unsecured and non-interest-bearing liabilities have been included as due to related parties in the accompanying consolidated balance sheets.

Other related party transactions are disclosed elsewhere in these notes to consolidated financial statements.

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8. OTHER CURRENT LIABILITIES

Other current liabilities were comprised of the following items:

	September 30, 2014	March 31, 2014
Accrued interest	\$570,741	\$1,165,335
Accrued legal fees	179,465	179,465
Accrued liquidated damages	362,800	362,800
Other accrued liabilities	103,598	147,774
Total other current liabilities	\$1,216,604	\$1,855,374

As of the date of this report, various promissory and convertible notes payable in the aggregate principal amount of \$473,422 (as identified in Notes 4 and 5 above) have reached maturity and are past due. We are continually reviewing other financing arrangements to retire all past due notes. At September 30, 2014, we had accrued interest in the amount of \$471,041 associated with these defaulted notes in accrued liabilities payable (see Notes 4 and 5).

9. FAIR VALUE MEASUREMENTS

We follow FASB ASC 820, "FAIR VALUE MEASUREMENTS AND DISCLOSURES" ("ASC 820") in connection with assets and liabilities measured at fair value on a recurring basis subsequent to initial recognition. The guidance applies to our derivative liabilities. We had no assets or liabilities measured at fair value on a non-recurring basis for any period reported.

ASC 820 requires that assets and liabilities carried at fair value will be classified and disclosed in one of the following three categories: We measure the fair value of applicable financial and non-financial assets based on the following fair value hierarchy:

Level 1: Quoted market prices in active markets for identical assets or liabilities.

Level 2: Observable market based inputs or unobservable inputs that are corroborated by market data.

Explanation of Responses:

Level 3: Unobservable inputs that are not corroborated by market data.

The hierarchy noted above requires us to minimize the use of unobservable inputs and to use observable market data, if available, when determining fair value.

The fair value of our recorded derivative liabilities is determined based on unobservable inputs that are not corroborated by market data, which is a Level 3 classification. We record derivative liabilities on our balance sheet at fair value with changes in fair value recorded in our consolidated statements of operations.

At September 30, 2014, we no longer had any derivative liabilities as all of the holders of the financial instruments that had price antidilution protection waived such price antidilution protection.

Our fair value measurements at the March 31, 2014 reporting date are classified based on the valuation technique level noted in the table below:

Description	March 31, 2014	Quoted Prices in Active Markets for (Level 1)	Significant Other Observable (Level 2)	Significant Unobservable (Level 3)
Derivative Liabilities	\$10,679,067	\$	– \$	– \$10,679,067
Total Assets	\$10,679,067	\$	– \$	– \$10,679,067

The following outlines the significant weighted average assumptions used to estimate the fair value information presented, in connection with our warrant and embedded conversion option derivative instruments utilizing the Binomial Lattice option pricing model:

The following outlines the significant weighted average assumptions used to estimate the fair value information presented, in connection with our warrant and embedded conversion option derivative instruments utilizing the Binomial Lattice option pricing model:

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Six Months Ended September 30, 2013

Risk free interest rate	0.02% - 0.62%
Average expected life	0.25 – 3 years
Expected volatility	78.9% - 104.5%
Expected dividends	None

The table below sets forth a summary of changes in the fair value of our Level 3 financial instruments for the six months ended September 30, 2014:

	April 1, 2014	Recorded New Derivative Liabilities	Change in estimated fair value recognized in results of operations	Reclassification of Derivative Liability to Paid in capital	September 30, 2014
Derivative liabilities	\$ 10,679,067	\$ –	\$ –	\$ (10,679,067)	\$ –

The table below sets forth a summary of changes in the fair value of our Level 3 financial instruments for the six months ended September 30, 2013:

	April 1, 2013	Recorded New Derivative Liabilities	Change in estimated fair value recognized in results of operations	Reclassification of Derivative Liability to Paid in capital	September 30, 2013
Derivative liabilities	\$ 3,588,239	\$ –	\$ 2,382,877	\$ (106,501)	\$ 5,864,615

10. STOCK COMPENSATION

The following table breaks out the components of our share-based compensation expenses relating to shares and options granted and the effect on basic and diluted loss per common share during the three and six months ended

Explanation of Responses:

September 30, 2014 and 2013.

	Three Months Ended September 30, 2014	Three Months Ended September 30, 2013	Six Months Ended September 30, 2014	Six Months Ended September 30, 2013
Vesting of stock options	89,793	73,856	260,680	124,243
Incremental fair value of option modifications	–	957	–	1,914
Vesting expense associated with CEO restricted stock grant	–	–	–	64,444
Total share-based compensation expense	\$89,793	\$74,813	\$260,680	\$190,601
Total share-based compensation expense included in net loss	\$89,793	\$73,856	\$260,680	\$190,601
Weighted average number of common shares outstanding – basic and diluted	259,369,911	187,643,582	243,494,916	182,004,220
Basic and diluted loss per common share	\$(0.00) \$(0.00) \$(0.00) \$(0.00

All of the stock-based compensation expense recorded during the six months ended September 30, 2014 and 2013, which totaled \$260,680 and \$190,601, respectively, is included in payroll and related expense in the accompanying condensed consolidated statements of operations. Stock-based compensation expense recorded during the six months ended September 30, 2014 and 2013 had no impact on basic and diluted loss per common share.

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We review share-based compensation on a quarterly basis for changes to the estimate of expected award forfeitures based on actual forfeiture experience. The cumulative effect of adjusting the forfeiture rate for all expense amortization is recognized in the period the forfeiture estimate is changed. The effect of forfeiture adjustments for the three and six month periods ended September 30, 2014 was insignificant.

On June 6, 2014, our Board of Directors approved the following grants of options to certain officers and directors of the Company:

To Mr. James A. Joyce, an option to acquire an aggregate of 1,500,000 shares of our common stock at an exercise price of \$0.19 per share, the closing price of our common stock on the date of grant. The fair value of this stock option at the date of grant was \$246,000. The option vested as to 500,000 shares on the grant date for a vesting expense of \$82,000 and will vest as to an additional 500,000 shares on each of the first two anniversaries of the grant date. Unless earlier exercised or terminated, the option will expire June 6, 2024.

To Mr. Rodney S. Kenley, an option to acquire an aggregate of 250,000 shares of our common stock at an exercise price of \$0.19 per share, the closing price of our common stock on the date of grant. The fair value of this stock option at the date of grant was \$41,000. The option vested as to 83,333 shares on the grant date for a vesting expense of \$13,667 and will vest as to an additional 83,333 shares on the first anniversary of the grant date and 83,334 shares on the second anniversary of the grant date. Unless earlier exercised or terminated, the option will expire June 6, 2024.

To Mr. James B. Frakes, an option to acquire an aggregate of 250,000 shares of our common stock at an exercise price of \$0.19 per share, the closing price of our common stock on the date of grant. The fair value of this stock option at the date of grant was \$41,000. The option vested as to 83,333 shares on the grant date for a vesting expense of \$13,667 and will vest as to an additional 83,333 shares on the first anniversary of the grant date and 83,334 shares on the second anniversary of the grant date. Unless earlier exercised or terminated, the option will expire June 6, 2024.

To Dr. Richard H. Tullis, an option to acquire an aggregate of 50,000 shares of our common stock at an exercise price of \$0.19 per share, the closing price of our common stock on the date of grant. The fair value of this stock option at the date of grant was \$8,200. The option vested as to 16,667 shares on the grant date for a vesting expense of \$2,733 and will vest as to an additional 16,667 shares on the first anniversary of the grant date and 16,666 shares on the second anniversary of the grant date. Unless earlier exercised or terminated, the option will expire June 6, 2024.

In addition to the above grants to our officers, on June 6, 2014, our Board of Directors also approved the grant of options to five employees to acquire an aggregate of 370,000 shares of our common stock at an exercise price of \$0.19 per share, the closing price of our common stock on the date of grant. The aggregate fair value of those stock options at the date of grant was \$60,680. Those options vested as to 123,333 shares on the grant date for a vesting expense of \$20,227 and will vest as to an additional 123,333 shares on the first anniversary of the grant date and 123,334 shares

on the second anniversary of the grant date. Unless earlier exercised or terminated, the option will expire June 6, 2024.

In addition to the share-based compensation expense for the specific stock option grants noted above, our total share-based compensation expense for the three and six months ended September 30, 2014 includes ongoing vesting expense associated with stock grants from prior periods.

Changes to 2012 Board Compensation Program

In July 2012, the Board approved a Board Compensation Program (the “2012 Program”), which modified and superseded the 2005 Directors Compensation Program that had been in effect previously. On June 6, 2014, the Board approved certain changes to the 2012 Program. Under the modified 2012 Program, in which only non-employee Directors may participate, a new eligible Director will receive an initial grant of \$50,000 worth of options to acquire shares of common stock, with such grant being valued at the exercise price based on the average of the closing bid prices of our common stock for the five trading days preceding the first day of the fiscal year. These options will have a term of ten years and will vest 1/3 upon grant and 1/3 upon each of the first two anniversaries of the date of grant.

At the beginning of each fiscal year, each existing Director eligible to participate in the 2012 Program also will receive a grant of \$35,000 worth of options valued at the exercise price based on the average of the closing bid prices of the Common Stock for the five trading days preceding the first day of the fiscal year. Such options will vest on the first anniversary of the date of grant. In lieu of per meeting fees, under the 2012 Program eligible Directors will receive an annual Board retainer fee of \$30,000. The modified 2012 Program also provides for the following annual retainer fees: Audit Committee Chair - \$5,000, Compensation Committee chair - \$5,000, Audit Committee member - \$4,000, Compensation Committee member - \$4,000 and Lead independent director - \$15,000.

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As a result of the modified 2012 Program on June 6, 2014, we issued 184,211 stock options to each of our three outside directors. Those grants vest over the fiscal year ending March 31, 2015 and have an exercise price of \$0.19 per share.

All of the foregoing actions - the changes in base salaries, the option grants and the changes to the Directors Compensation Program discussed herein - were approved and recommended by the Company's Compensation Committee prior to approval by the Board.

The following outlines the significant weighted average assumptions used to estimate the fair value information presented, with respect to stock option grants utilizing the Binomial Lattice option pricing models at, and during the six months ended September 30, 2014:

Risk free interest rate	2.6%
Average expected life	10 years
Expected volatility	90.23%
Expected dividends	None

The expected volatility was based on the historic volatility. The expected life of options granted was based on the "simplified method" as described in the SEC's guidance due to changes in the vesting terms and contractual life of current option grants compared to our historical grants.

In May 2013, we granted to a scientific advisory board member and a scientific consultant a three year option to purchase 125,000 shares of our common stock at a price of \$0.11 per share.

In July 2013, our compensation committee and Board of Directors approved the issuance of four stock option grants to four of our executives. The options carried an exercise price of \$0.10 per share, have a ten year life and vest over the following schedule: 25% on July 1, 2014, 25% on July 1, 2015, 25% on July 1, 2016 and 25% on July 1, 2017. The numbers of shares underlying each of the stock option grants were as follows: 2,000,000 shares to our chief executive officer and 500,000 shares each to our president, chief science officer and chief financial officer (see Note 10).

The following outlines the significant weighted average assumptions used to estimate the fair value information, which is based on historical data, with respect to stock option grants utilizing the Binomial Lattice option pricing models at, and during the six months ended September 30, 2013:

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Risk free interest rate	0.38% - 2.50%
Average expected life	3 years - 10 years
Expected volatility	94.6% - 102.7%
Expected dividends	None

The expected volatility was based on the historic volatility. The expected life of options granted was based on the "simplified method" as described in the SEC's guidance due to changes in the vesting terms and contractual life of current option grants compared to our historical grants.

Options outstanding that have vested and are expected to vest as of September 30, 2014 are as follows:

	Number of Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term in Years
Vested	24,294,227	\$ 0.26	3.96
Expected to vest	4,711,811	\$ 0.14	9.15
Total	29,006,038		

A summary of stock option activity during the six months ended September 30, 2014 is presented below:

	Number of Options	Range of Exercise Price	Weighted Average Exercise Price
Stock options outstanding at March 31, 2014	26,133,407	\$0.076 - \$0.41	\$ 0.25
Exercised	—	—	—
Granted	2,972,631	0.19	\$ 0.19
Cancelled/Expired	(100,000)	0.19	0.19
Stock options outstanding at September 30, 2014	29,006,038	\$0.076 - \$0.41	\$ 0.24
Stock options exercisable at September 30, 2014	24,294,227	\$0.076 - \$0.41	\$ 0.26

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At September 30, 2014, there was approximately \$497,783 of unrecognized compensation cost related to share-based payments, which is expected to be recognized over a weighted average period of 2.19 years.

On September 30, 2014, our stock options had a negative intrinsic value since the closing price of our common stock on that date of \$0.12 per share was below the weighted average exercise price of our stock options.

11. WARRANTS

A summary of warrant activity during the six months ended September 30, 2014 is presented below:

	Amount	Range of Exercise Price	Weighted Average Exercise Price
Warrants outstanding at March 31, 2014	70,709,475	\$0.042 - \$0.25	\$ 0.13
Exercised	(2,166,104)	\$0.086 - \$0.12	\$ 0.10
Issued	15,375,614	\$0.042 - \$0.24	\$ 0.07
Cancelled/Expired	(1,136,364)	\$0.13	\$ 0.13
Warrants outstanding at September 30, 2014	82,782,621	\$0.042 - \$0.25	\$ 0.10
Warrants exercisable at September 30, 2014	82,782,621	\$0.042 - \$0.25	\$ 0.10

The following outlines the significant weighted average assumptions used to estimate the fair value information presented, with respect to warrants utilizing the Binomial Lattice option pricing models at, and during, the six months ended September 30, 2014:

Risk free interest rate	0.79% - 2.29%
Average expected life	5 years - 7 years
Expected volatility	90.1% - 95.8%
Expected dividends	None

12. DARPA CONTRACT AND RELATED REVENUE RECOGNITION

As discussed in Note 1, we entered into a contract with the DARPA on September 30, 2011. Under the DARPA award, we have been engaged to develop a therapeutic device to reduce the incidence of sepsis, a fatal bloodstream infection that often results in the death of combat-injured soldiers. The award from DARPA was a fixed-price contract with potential total payments to us of \$6,794,389 over the course of five years. Fixed price contracts require the achievement of multiple, incremental milestones to receive the full award during each year of the contract. Under the terms of the contract, we will perform certain incremental work towards the achievement of specific milestones against which we will invoice the government for fixed payment amounts.

Originally, only the base year (year one contract) was effective for the parties, however, DARPA subsequently exercised the option on the second, third and fourth years of the contract. DARPA has the option to enter into the contract for year five. The milestones are comprised of planning, engineering and clinical targets, the achievement of which in some cases will require the participation and contribution of third party participants under the contract. There can be no assurance that we alone, or with third party participants, will meet such milestones to the satisfaction of the government and in compliance with the terms of the contract or that we will be paid the full amount of the contract revenues during any year of the contract term. We commenced work under the contract in October 2011.

Due to budget restrictions within the Department of Defense, on February 10, 2014, DARPA reduced the scope of our contract in years three through five of the contract. The reduction in scope focused our research on exosomes, viruses and blood processing instrumentation. This scope reduction will reduce the possible payments under the contract by \$858,491 over years three through five. We recently completed a re-budgeting of the expected costs on the remaining years of the DARPA contract based on the reduced milestones and have concluded that the reductions in our costs due to the scaled back level of work will almost entirely offset the anticipated revenue levels based on current assumptions.

During the six months ended September 30, 2014, we invoiced DARPA for three milestones totaling \$444,723. The details of those milestones were as follows:

Milestone 2.4.2.2 – Determine capacity requirements of affinity resin to multiple simultaneous targets. The milestone payment was \$197,362. Management considers this milestone to be substantive as it was not dependent on the passage of time nor was it based solely on another party's efforts. We demonstrated that we were able to determine the capacity requirements of affinity resin to multiple simultaneous targets. The report was accepted by the contracting officer's representative and the invoice was submitted thereafter.

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Milestone 2.4.2.4 – Finish construction and delivery of 25 experimental cartridges for testing by the system integrator. The milestone payment was \$50,000. Management considers this milestone to be substantive as it was not dependent on the passage of time nor was it based solely on another party's efforts. We demonstrated that we delivered the 25 cartridges to the systems integrator as part of our submission for approval. The report was accepted by the contracting officer's representative and the invoice was submitted thereafter.

Milestone M9 – Target capture > 90% in 24 hours for at least 3 targets ex vivo in blood or blood components using the optimized cartridge. The milestone payment was \$197,361. Management considers this milestone to be substantive as it was not dependent on the passage of time nor was it based solely on another party's efforts. We demonstrated that we were able to capture approximately 90% in 24 hours for at least 3f targets ex vivo in blood or blood components using the optimized cartridge. The report was accepted by the contracting officer's representative and the invoice was submitted thereafter.

In the six months ended September 30, 2013, we invoiced DARPA for four milestones totaling \$808,739. The details of those milestones were as follows:

Milestone 2.3.2.2 – Formulate initial design work based on work from the previous phase. Begin to build and test selected instrument design and tubing sets. The milestone payment was \$195,581. Management considers this milestone to be substantive as it was not dependent on the passage of time nor was it based solely on another party's efforts. We demonstrated that we were able to formulate the initial design work and to build and test selected instrument design and tubing sets as part of our submission for approval. The report was accepted by the contracting officer's representative and the invoice was submitted thereafter.

Milestone 2.3.2.2 – Write and test software and conduct ergonomic research. Begin discussions with the systems integrator. The milestone payment was \$195,581. Management considers this milestone to be substantive as it was not dependent on the passage of time nor was it based solely on another party's efforts. We obtained wrote and tested software and conducted ergonomic research and began discussions with the systems integrator. The report was accepted by the contracting officer's representative and the invoice was submitted thereafter.

Milestone 2.3.3.2 – Cartridge construction with optimized affinity matrix design for each potential target. Complete the capture agent screening. The milestone payment was \$208,781. Management considers this milestone to be substantive as it was not dependent on the passage of time nor was it based solely on another party's efforts. We completed the cartridge construction with optimized affinity matrix design for each potential target and completed the capture agent screening. The report was accepted by the contracting officer's representative and the invoice was submitted thereafter.

Milestone M5 – Target capture > 90% in 24 hours for at least three targets in blood or blood components. The milestone payment was \$208,781. Management considers this milestone to be substantive as it was not dependent on the passage of time nor was it based solely on another party's efforts. We demonstrated that we were able to capture approximately 90% in 24 hours for at least three of the agreed targets in blood or blood components. The report was accepted by the contracting officer's representative and the invoice was submitted thereafter.

13. COMMITMENTS AND CONTINGENCIES

LEASE COMMITMENTS

We rented approximately 2,300 square feet of executive office space at 8910 University Center Lane, Suite 660, San Diego, CA 92122 at the rate of \$6,475 per month on a four year lease that expired in September 2014. We continued leasing that space for the month of October and, effective November 1, 2014, moved into a new facility of approximately 2,576 square feet located at 9635 Granite Ridge Drive, San Diego, CA 92123 under a 39 month lease with an initial rental rate of \$6,054 per month. We believe this new leased facility will be satisfactory for our office needs over the term of the lease.

We also rent approximately 1,700 square feet of laboratory space at 11585 Sorrento Valley Road, Suite 109, San Diego, California 92121 at the rate of \$3,917 per month on a one year lease that previously was scheduled to expire in October 2014 and was recently extended to in October 2015. We believe this new leased facility will be satisfactory for our laboratory needs over the term of the lease

Our Exosome Sciences, Inc. subsidiary rents approximately 2,055 square feet of office and laboratory space at 11 Deer Park Drive, South Brunswick, NJ at the rate of \$3,596 per month on a one year lease that previously was scheduled to expire in October 2014 and was recently extended to in October 2015. We believe this new leased facility will be satisfactory for ESI's operational needs over the term of the lease.

Rent expense approximated \$84,000 and \$68,000 for the six month periods ended September 30, 2014 and 2013, respectively.

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LEGAL MATTERS

From time to time, claims are made against us in the ordinary course of business, which could result in litigation. Claims and associated litigation are subject to inherent uncertainties and unfavorable outcomes could occur, such as monetary damages, fines, penalties or injunctions prohibiting us from selling one or more products or engaging in other activities.

The occurrence of an unfavorable outcome in any specific period could have a material adverse effect on our results of operations for that period or future periods. Other than as mentioned here, we are not presently a party to any pending or threatened legal proceedings.

14. SEGMENTS

We operate our businesses principally through two reportable segments: Aethlon, which represents our therapeutic business activities, and ESI, which represents our diagnostic business activities. Our reportable segments have been determined based on the nature of the potential products being developed. ESI did not have any operations in the six months ended September 30, 2013.

Aethlon's revenue is generated primarily from government contracts to date and ESI does not yet have any revenues. We have not included any allocation of corporate overhead to the ESI segment.

The following tables set forth certain information regarding our segments and other operations that conforms to the consolidated balance sheet and statement of operations presented in this Report:

	Six Months Ended September 30,	
	2014	2013
Revenues:		
Aethlon	\$ 530,371	\$ 840,483
ESI	—	—
Total Revenues	\$ 530,371	\$ 840,483
Operating Losses:		
Aethlon	\$(1,294,453)	\$(1,013,592)

Explanation of Responses:

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ESI	(445,674)	–
Total Operating Loss	\$(1,773,200)	\$(1,013,592)

Net Losses:

Aethlon	\$(4,202,873)	\$(3,653,168)
ESI	(356,539)	–
Net Loss Before Non-Controlling Interests	\$(4,592,485)	\$(3,653,168)

Cash:

Aethlon	\$47,865	\$8,754
ESI	478,322	–
Total Cash	\$526,187	\$8,754

Total Assets:

Aethlon	\$443,027	\$411,190
ESI	646,242	–
Total Assets	\$1,089,269	\$411,190

Capital Expenditures:

Aethlon	\$–	\$–
ESI	–	–
Capital Expenditures	\$–	\$–

Depreciation and Amortization:

Aethlon	\$8,885	\$4,727
ESI	9,791	–
Total Depreciation and Amortization	\$18,676	\$4,727

Interest Expense:

Aethlon	\$156,799	\$216,502
ESI	–	–
Total Interest Expense	\$156,799	\$216,502

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15. SUBSEQUENT EVENTS

Management has evaluated events subsequent to September 30, 2014 through the date that the accompanying condensed consolidated financial statements were filed with the Securities and Exchange Commission for transactions and other events which may require adjustment of and/or disclosure in such financial statements.

Government Contracts

Subsequent to September 30, 2014, we collected \$247,361 under our DARPA contract, and under the Battelle subcontract we billed \$33,434 and we collected \$29,519.

Debt Reduction

Subsequent to September 30, 2014, we paid off the remaining principal and interest balances on the two remaining July & August 2011 10% Convertible Notes, which had been classified as being in default, with cash payments totaling \$382,748 (see Note 5).

Subsequent to September 30, 2014, we paid off in full the outstanding principal balance and interest balance on the Law Firm Note with a cash payment of \$50,000 and an issuance of 170,020 common shares (see Note 5).

Subsequent to September 30, 2014, we paid an aggregate of \$503,313 in principal and accrued interest on eight other outstanding notes. As a result, seven of the eight notes were paid in full. We owe an additional \$37,813 under the eighth note, which we expect to pay in full in January 2015.

Note Conversions

Subsequent to September 30, 2014, we issued an aggregate of 14,237,261 shares of common stock to two accredited investors upon the conversion of an aggregate of \$597,965 of unpaid principal and accrued interest due under promissory notes previously issued to the investors by the Company. The conversion price per share was \$0.042.

Subsequent to September 30, 2014, we issued an aggregate of 5,625,000 shares of common stock to convert in full the outstanding principal balance of \$225,000 and interest balance of \$11,250 on the remaining Amended and Restated Series A 12% Convertible Note through the issuance of 5,625,000 shares of common stock. The conversion price per share was \$0.042.

Issuance of Convertible Notes

Subsequent to September 30, 2014, we entered into a Subscription Agreement with two accredited investors providing for the issuance and sale of (i) convertible promissory notes in the aggregate principal amount of \$527,780 and (ii) five year warrants to purchase up to 2,356,160 shares of common stock at a fixed exercise price of \$0.168 per share. The convertible promissory notes bear interest at the annual rate of 10% and mature on April 1, 2016. The aggregate gross cash proceeds to us were \$415,000 after subtracting legal fees of \$35,000; the balance of the principal amount of the notes represents a \$27,780 due diligence fee and an original issuance discount. The convertible promissory notes are convertible at the option of the holders into shares of our common stock at a fixed price of \$0.112 per share, for up to an aggregate of 4,712,321 shares of common stock. There are no registration requirements with respect to the shares of common stock underlying the notes or the warrants.

Common Stock Issuances

Subsequent to September 30, 2014, we issued 374,295 shares of common stock pursuant to our S-8 registration statement covering our Amended 2010 Stock Plan at an average price of \$0.146 per share in payment for legal and scientific consulting services valued at \$54,800 based on the value of the services provided.

Equity Unit Investments

Subsequent to September 30, 2014, we issued and sold to eight accredited investors units (the "Units") consisting of (a) one hundred thousand (100,000) restricted shares of common stock, par value \$.001 per share at prices per share ranging from \$0.105 to \$0.114 and (b) a five-year warrant to purchase fifty thousand (50,000) shares of common stock at exercise prices ranging from \$0.154 to \$0.167 per share (the "Unit Warrants"). In total, the investors purchased for cash an aggregate of \$501,700 of Units. The investors acquired an aggregate of 4,506,250 shares of common stock and Unit Warrants to acquire up to an aggregate of 2,253,125 shares of common stock.

Subsequent to September 30, 2014, we issued to an accredited investor Units consisting of an aggregate of 1,835,798 shares of common stock and Unit Warrants to acquire up to an aggregate of 1,837,798 shares of common stock at an exercise price of \$0.103 per share. The Units were issued to the investor upon the conversion of an aggregate of \$189,087 of unpaid principal and accrued interest due under two promissory notes (the remaining October & November 2009 10% Convertible Note and the April 2010 10% Convertible Note – see Note 5) previously issued to the investor by the Company. The amounts converted represented the entire principal and interest outstanding under the notes and the notes held by that holder were retired.

Subsequent to September 30, 2014, we sold \$3,300,000 of units, comprised of common stock and warrants (the “Units”), to three affiliated institutional investors (collectively the “Purchaser”) at a price of \$0.30 per Unit pursuant to a Securities Purchase Agreement (the “Agreement”). Each Unit consists of one share of common stock, \$0.001 par value per share, and five-year warrants to purchase 120% of the shares of common stock in the Unit (the “Warrants”), at an exercise price per share of \$0.30 (the “Financing”). Accordingly, a total of 11,000,000 shares of common stock and Warrants to purchase 13,200,000 shares of common stock were issued and sold pursuant to the Agreement.

As part of the terms of the Agreement, we entered into a Registration Rights Agreement with the Purchaser pursuant to which we agreed to file a registration statement to register for resale the shares of common stock sold in the Financing, including the shares of common stock underlying the Warrants, within 20 calendar days following the closing of the Financing. Subject to certain exceptions, in the event the registration statement does not become effective within certain time periods set forth in the Registration Rights Agreement, we would be required to pay the Purchaser in the Financing an amount in cash equal to two percent (2.0%) of the aggregate purchase price every month until such time as the registration statement becomes effective or the shares of common stock (and shares of common stock underlying the Warrants) sold in the Financing may be sold by the Purchaser pursuant to Rule 144 without any restrictions or limitations.

Roth Capital Partners served as sole placement agent for the Financing and received a cash fee of \$231,000, expense reimbursement of \$25,000, and a five-year warrant to purchase 550,000 shares of common stock at an exercise price of \$0.30 per share (the “Purchase Agent Warrant”) for its services in the Financing. In addition, we paid \$10,000 in legal expenses to the Purchaser’s counsel. We also paid \$32,572 to our counsel related to this financing. The net proceeds to us after the placement fee and legal fees were \$3,001,429.

Warrant Exercises and Issuance of New Warrants Upon Exercise

Subsequent to September 30, 2014, we issued an aggregate of 5,671,119 shares of common stock and seven-year warrants (the “Exchange Warrants”) to issue up to an aggregate of 5,671,119 shares of common stock at exercise prices ranging from \$0.093 to \$0.116 per share to eight accredited investors. One of the investors is Dr. Chetan Shah, a director of the Company. The common stock and Exchange Warrants were issued to the investors upon the cash

exercise of previously issued warrants held by them. The investors paid an aggregate of \$579,251 upon exercise of the previously outstanding warrants at exercise prices ranging from \$0.093 to \$0.115 per share. The foregoing transaction was privately negotiated with the group of participating warrant holders.

Warrant Exercises

Subsequent to September 30, 2014, we issued an aggregate of 21,516,640 shares of common stock to accredited investors upon the exercise of previously issued warrants. The warrants were exercised on a cashless or “net” basis. Accordingly, we did not receive any proceeds from such exercises. The cashless exercise of such warrants resulted in the cancellation of previously issued warrants to purchase an aggregate of 30,265,208 shares of common stock.

Stock Option Exercises

Subsequent to September 30, 2014, two former employees exercised stock options to purchase 50,000 common shares through a cash payment of \$9,500 with an exercise price of \$0.19 per share.

Restricted Stock Issuance to Service Provider

Subsequent to September 30, 2014, we issued 39,024 shares of restricted common stock in payment for investor relations services valued at \$8,000 based on the value of the services provided.

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