ARISTOTLE CORP
Form 10-Q
August 14, 2002

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

(MARK ONE)

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

FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2002

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

FOR THE TRANSITION PERIOD FROM ____________________ TO ______________

COMMISSION FILE NUMBER 0-14669

THE ARISTOTLE CORPORATION
(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

DELAWARE
(STATE OR OTHER JURISDICTION OF INCORPORATION OR ORGANIZATION)

96 CUMMINGS POINT RD., STAMFORD, CONNECTICUT
(ADDRESS OF PRINCIPAL EXECUTIVE OFFICES)

06-1165854
(I.R.S. EMPLOYER IDENTIFICATION NO.)

06902
(ZIP CODE)

REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE:
(203) 867-4090

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes [X] No

As of August 10, 2002, 17,031,687 shares of Common Stock, 1,046,716 shares of Series I Preferred Stock and 10,984,971 shares of Series J Preferred Stock were outstanding.

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THE ARISTOTLE CORPORATION

INDEX OF INFORMATION CONTAINED IN FORM 10-Q FOR THE QUARTER ENDED JUNE 30, 2002

PART I - FINANCIAL INFORMATION

PART II - OTHER INFORMATION

THE ARISTOTLE CORPORATION AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS
(DOLLARS IN THOUSANDS, EXCEPT FOR SHARE DATA)

	J

ASSETS	(UN

Current assets:	
Cash and cash equivalents..	$
Marketable securities..	

Accounts receivable, net	
Inventories	
Deferred income taxes	
Other current assets	
Total current assets	
Property, plant and equipment, net	
Other assets:	
Goodwill, net	
Deferred income taxes	
Other noncurrent assets	
Total other assets	
Total assets	$
LIABILITIES AND STOCKHOLDERS' EQUITY	
Current liabilities:	
Current maturities of long term debt	$
Accounts payable	
Accounts payable, affiliates	
Accrued expenses	
Accrued dividends payable	
Accrued income taxes	
Deferred revenue	
Total current liabilities	
Long term debt, net of current maturities	
Total liabilities	
Stockholders' equity:	
Preferred Stock, Series I, $6.00 stated value, $.01 par value, 2,400,000 shares authorized, 1,046,716 issued and outstanding	
Preferred Stock, Series J, $6.00 stated value, $.01 par value, 11,200,000 shares authorized, 10,984,971 issued and outstanding	
Common stock, $.01 par value, 20,000,000 shares authorized, 17,044,675 shares issued and 17,031,687 shares outstanding as of June 2002 and 15,000,000 shares deemed issued as of December 2001; 12,988 shares of treasury stock as of June 30,2002	
Additional paid-in capital	
Retained earnings	
Accumulated other comprehensive loss	
Total stockholders' equity	
	$

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

THE ARISTOTLE CORPORATION AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)
(DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)

	THREE MONTHS ENDE JUNE 30, 2002	20
Net revenue	$ 43,322	$ 43
Cost of goods sold	27,987	28
Gross profit	15,335	14
Selling, general and administrative expenses	10,053	9
Special charges-American Educational Products, Inc. (AMEP)	--	
Operating income	5,282	4
Other income (expense):		
Investment interest and other, net	(8)	
Interest expense	(508)	
Income before income taxes, minority interest and extraordinary gain	4,766	3
Provision for income taxes	(1,940)	(1
Income before minority interest and extraordinary gain	2,826	2
Minority interest	--	
Extraordinary gain	20,237	
Net income	23,063	2
Preferred dividends	306	
Net income applicable to common shareholders	$ 22,757	$ 2
Basic earnings per common share:		
Income before extraordinary gain	$ .16	$
Extraordinary gain	1.33	
Net Income	$ 1.49	$
Diluted earnings per common share:		
Income before extraordinary gain	$ .16	$
Extraordinary gain	1.31	
Net income	$ 1.47	$

Weighted average shares outstanding:		
Basic shares	15,290,241	15,000
Diluted shares	15,518,106	15,000

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

THE ARISTOTLE CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)
(DOLLARS IN THOUSANDS)

Cash flows from operating activities:	
Net income applicable to common shareholders	$
Adjustments to reconcile net income available to common shareholders to net cash provided by(used in) operating activities:	
Extraordinary gain	
Depreciation and amortization	
Stock option compensation expense	
Loss on sale or disposal of property, plant and equipment	
Effect of inventory purchase adjustment	
Change in assets and liabilities, net of effects of acquired business:	
Accounts receivable	
Inventories	
Prepaid expenses and other current assets	
Trade accounts payable	
Accrued expenses	
Intangible assets and other non-current assets	
Net cash provided by (used in) operating activities	
Cash flows from investing activities:	
Purchases of property, plant and equipment	
Proceeds from the sale of property, plant and equipment	
Cash acquired in merger with Nasco International, Inc.	
Cash paid for acquisition of AMEP interest	
Cash paid for acquisition of Spectrum, net of cash acquired	
Net cash provided by (used in) investing activities	
Cash flows from financing activities:	
Equity contribution from parent	
Payments on line of credit	
Proceeds from issuance of long term debt	
Payment of Geneve notes payable	
Principal payments on long-term debt	

Net cash (used in) provided by financing activities		
Net increase in cash and cash equivalents		
Cash and cash equivalents at beginning of period		
Cash and cash equivalents at end of period	$	
Supplemental disclosures of cash flow information:		
Cash paid during the period for:		
Interest	$	
Income taxes	$	

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

THE ARISTOTLE CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2002
(UNAUDITED)

1. NATURE OF OPERATIONS AND BASIS OF PRESENTATION

Prior to June 17, 2002, The Aristotle Corporation ("Aristotle" or the "Company") was a holding company which, through its subsidiaries, Simulaids, Inc. ("Simulaids") and Safe Passage International, Inc. ("Safe Passage"), conducted business in two segments, the medical education and training products market and the computer-based training market. Simulaids' primary products include manikins and simulation kits used for training in CPR, emergency rescue and patient care fields. Simulaids' products are sold throughout the United States and internationally via distributors and catalogs to end users such as fire and emergency medical departments and nursing and medical schools. Safe Passage develops and licenses computer-based training products to government and industry clients.

On June 17, 2002, Aristotle merged (the "Merger") with Nasco International, Inc. ("Nasco"), an indirect subsidiary of the Geneve Corporation, a privately-held diversified financial services company ("Geneve"). In connection with the Merger, Aristotle changed its accounting fiscal year from a June 30th year-end to a December 31st year-end.

Nasco is a leading manufacturer and global catalog-distribution company serving the education, health and agriculture markets. A selection of over 80,000 items is offered, primarily through catalogs carrying the brand of Nasco, as well as those bearing the brands of Triarco, Summit Learning, Hubbard Scientific, Scott Resources and Spectrum Educational Supplies. Products include educational materials and supplies for substantially all K-12 curricula, molded plastics, biological materials and items for the agriculture, senior care and food industries. Simulaids, Inc. and Nasco, combine to offer simulation kits and manikins used for training in cardiopulmonary resuscitation, and the fire and emergency rescue and patient care fields.

Pursuant to the Merger, on June 17, 2002, the separate corporate existence of Nasco ceased and Aristotle was the surviving entity. Immediately following the Merger, Aristotle's business was comprised of the operations of the Nasco group of companies, Simulaids and Safe Passage. Due to the relative sizes of the parties and conditions to the Merger, the transaction was accounted for as a reverse acquisition using the purchase method of accounting under accounting principles generally accepted in the United States of America. Accordingly, for accounting and reporting purposes, Nasco is deemed to be the acquiring company and financial information reported for periods prior to the Merger is that of Nasco. In applying purchase accounting to the Merger, the assets and liabilities of Aristotle were adjusted to their fair market values at June 17, 2002. This included recognition of a significant deferred tax asset principally attributable to Aristotle's net operating loss carryforwards. As a result of such recognition, Aristotle's non-current assets were reduced to zero and negative goodwill of $20.2 million was recognized as an extraordinary gain at the acquisition date.

As consideration for the Merger, Nasco Holdings Inc. ("Nasco Holdings"), the sole shareholder of Nasco and a subsidiary of Geneve received 15,000,000 shares of Aristotle's common stock and 10,000,000 shares of a newly authorized Series J $6.00 non-convertible, non-voting, cumulative 12% preferred stock, par value $0.01 per share. Separately, Aristotle paid a stock dividend of one share of newly authorized Series I $6.00 convertible, voting, cumulative 11% preferred stock, par value $0.01 per share on each share of Aristotle's common stock outstanding on June 10, 2002.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and do not include all of the information and notes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the six months ended June 30, 2002 are not necessarily indicative of results that may be expected for any other interim period or for the year ending December 31, 2002. For further information, refer to the consolidated financial statements and notes included in Aristotle's Proxy Statement-Prospectus dated May 15, 2002, Annual Report on Form 10-K for the year ended June 30, 2001 and quarterly reports on Form 10-Q for the quarterly periods ended September 30, 2001, December 31, 2001 and March 31, 2002.

2. PRO FORMA FINANCIAL DATA

The pro forma financial data and accompanying notes set forth below, which are unaudited, should be read in conjunction with the Consolidated Financial Statements and related notes included in this Quarterly Report on Form 10-Q and in Aristotle's Proxy Statement - Prospectus dated May 15, 2002, and Aristotle's 2001 Annual Report on Form 10-K previously filed with the Securities and Exchange Commission. The pro forma financial data is provided for informational purposes only and should not be construed to be indicative of Aristotle's financial condition or results of operations had the Merger been consummated on the dates assumed, and is not intended to project Aristotle's financial condition on any future date or results of operations for any future period.

The assumptions used in preparing this pro forma data are comparable to the assumptions described in the notes to the pro forma statements of operations and the pro forma balance sheet set forth later in this footnote. Operating results for the three and six months ended June 30, 2002 and 2001, on a pro forma basis as though Aristotle was acquired by Nasco on January 1, 2001, are summarized below.

	Three Months Ended June 30, (unaudited) (dollars in thousands, except p		
	2002	2001	
Net revenue	$45,175	$45,001	$
Net income applicable to common shareholders, before extraordinary gain	$ 1,098	$ 318	$
Basic earnings per common share, before extraordinary gain	$ .06	$ .02	$
Diluted earnings per common shares, before extraordinary gain	$ .06	$ .02	$

The following pro forma statements of operations for the six months ended June 30, 2002 and the twelve months ended December 31, 2001 reflect the historical accounts of Nasco and Aristotle, adjusted to give pro forma effect to the Merger and the stock dividend issuance as if those transactions had occurred at the beginning of the respective periods. The gain resulting from the generation of negative goodwill in the Merger does not appear in the pro forma statements of operations because it is considered extraordinary. The pro forma data for 2001 also reflects the Nasco's acquisition of Spectrum Educational Supplies Ltd, ("Spectrum") as if such acquisition had occurred at the beginning of the period.

Also set forth below is an unaudited pro forma balance sheet as of December 31, 2001, reflecting the historical accounts of Nasco and Aristotle as of that date, adjusted to give pro forma effect to the Merger (and the stock dividend which occurred simultaneously), as if they had been consummated on December 31, 2001.

THE ARISTOTLE CORPORATION
PRO FORMA STATEMENT OF OPERATIONS
FOR THE SIX MONTHS ENDED JUNE 30, 2002
(DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)
(UNAUDITED)

	Nasco Historical	Aristotle Historical	Purchase of Aristotle	
	(a)	(b)	(c)	
Net Revenues	$ 77,851	$ 5,164	$ (1,594)	(1
Cost of goods sold	50,264	2,519	(1,533)	(2
Gross profit (loss)	27,587	2,645	(61)	

Selling, general and administrative expenses	19,518	1,855	(1,039) (3
Operating income	8,069	790	978
Investment interest and other, net	17	(12)	-
Interest expense	(966)	(344)	
Income before income taxes	7,120	434	978
Provisions for income taxes	(2,842)	(190)	(374) (
Net income	4,278	244	604
Preferred dividends	306	-	3,994 (5
Net income applicable to common shareholders	$ 3,972	$ 244	$ (3,390)
Basic earnings per common share	0.26		
Diluted earnings per common share	0.26		
Weighted average shares outstanding:			
Basis shares	15,145,922		
Diluted shares	15,373,787		

(a) Represents amounts reported in this Quarterly Report on Form 10-Q for the six months ended June 30, 2002 for Nasco as the accounting acquirer (for the entire period) and for Aristotle (for the period subsequent to the Merger).
(b) Represents amounts for Aristotle prior to the Merger.
(c) Footnotes to Pro Forma Statement of Operations.

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FOOTNOTES TO PRO FORMA STATEMENT OF OPERATIONS
FOR THE SIX MONTHS ENDED JUNE 30, 2002
(DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)
(UNAUDITED)

(1) The elimination of intercompany sales between Nasco and Aristotle.
(2) The elimination of intercompany transactions between Nasco and Aristotle of $1,478 and the reduction in depreciation and amortization expense of $55 due to the elimination of all Aristotle long-term assets.
(3) The elimination of Nasco Holdings' management fees paid by Nasco of $854, the elimination of intercompany transactions of $116 between Nasco and Aristotle and the reduction in depreciation and

amortization expense of $69 due to the elimination of Aristotle long-term assets.

(4) Recognition of an effective tax rate as a result of the balance sheet recognition of the deferred tax asset of $30,500 related to the future utilization of net operating loss carryforwards.

(5) To record dividends on the preferred stock: 1,046,716 shares of Series I $6.00 preferred stock with an 11% dividend. The Series I preferred stock represents the shares distributed to the non-Geneve shareholders on

the date of the closing of the Merger......................	$321
10,984,971 shares of Series J $6.00 Preferred Stock with a 12% dividend. The Series J Preferred Stock represents 984,971 shares distributed to Geneve on the date of the closing of the Merger and 10,000,000 shares received by Nasco Holdings as part of the exchange for its shares of Nasco's Common Stock	3,673
Total..	$3,994

Dividends are subject to the discretion of the Aristotle Board of Directors and will be affected in part by future financial performance, available cash and restrictions on cash dividends as set forth in credit agreements which have been entered into by Nasco and assumed by Aristotle.

THE ARISTOTLE CORPORATION
PRO FORMA RESULTS OF OPERATIONS
FOR THE TWELVE MONTHS ENDED DECEMBER 31, 2001
(DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)
(UNAUDITED)

	Nasco Historical	Nasco Acquisitions	Aristotle Historical	Pur of A
Net revenues................................	$161,961	$1,769(1)	$9,203	$(2
Cost of goods sold..........................	105,447	1,049(2)	4,639	(1
Gross profit (loss).........................	56,514	720	4,564	
Selling, general and administrative expenses..	38,207	720(3)	3,930	(1
Special charges--American Educational Products, Inc. (AMEP).......................	612	--	--	
Goodwill amortization.......................	455	43(4)	239	
Total operating expenses....................	39,274	763	4,169	(2
Operating income (loss).....................	17,240	(43)	395	1
Investment interest and other, net...........	455	--	219	

Interest expense	(3,159)	(58)(5)	(69)	
Income (loss) before income taxes and minority interest	14,536	(101)	545	
(Provision) benefit for income taxes	(5,860)	22 (6)	(71)	
Income (loss) before minority interest	8,676	(79)	474	
Minority interest	99	--	--	
Net income	8,775	(79)	474	
Preferred dividends	--	--	--	
Net income (loss) applicable to common shareholders	$8,775	$(79)	$474	$(
Basic earnings per common share	$ 0.52			
Diluted earnings per common share	$ 0.52			
Weighted average shares outstanding:				
Basic shares	16,931,581			
Diluted shares	16,977,104			

FOOTNOTES TO PRO FORMA STATEMENT OF OPERATIONS
FOR THE TWELVE MONTHS ENDED DECEMBER 31, 2001
(DOLLARS IN THOUSANDS)
(UNAUDITED)

(1) To record the historical sales of Spectrum of $1,801 for the three months ended March 31, 2001, to include results prior to Nasco's acquisition of Spectrum, partially offset by the elimination of intercompany sales of $32 between Spectrum and Nasco.
(2) To record the historical cost of sales of Spectrum of $1,801 for the three months ended March 31, 2001, partially offset by the elimination of intercompany costs between Aristotle and Nasco of $752.
(3) To record the expenses of Spectrum of $720 for the three months ended March 31, 2001.
(4) To record goodwill amortization related to Nasco's acquisition of Spectrum.
(5) To record interest costs incurred related to Nasco's acquisition of Spectrum.
(6) To record the income tax benefit related to costs incurred in Nasco's acquisition of Spectrum.
(7) The elimination of intercompany sales between Nasco and Aristotle.
(8) The elimination of intercompany transactions between Nasco and Aristotle of $1,911, additional costs of $631 resulting from the increase in the historical carrying value of the inventory and the resulting sale of such inventory in the twelve months ended December 31, 2001, and the reduction in depreciation and amortization expense of $114 due to the elimination of all Aristotle long-term assets.
(9) The elimination of management fees paid by Nasco to Nasco Holdings, Inc. of $1,612, the elimination of intercompany transactions of $143 between Nasco and Aristotle and the reduction in depreciation and amortization expense of $159 due to the elimination of Aristotle long-term assets.

(10) The reduction in amortization expense due to the elimination of Aristotle goodwill resulting from the application of purchase accounting to the assets and liabilities of Aristotle.

(11) Recognition of an effective tax rate as a result of the balance sheet recognition of the deferred tax asset of $33,200 related to the future utilization of net operating loss carryforwards.

(12) To record dividends on the preferred stock: 946,610 shares of Series I $6.00 Preferred Stock with an 11% dividend. The Series I Preferred Stock represents the shares distributed to the non-Geneve shareholders on the date of the closing of the Merger................................ $625
10,984,971 shares of Series J $6.00 Preferred Stock with a 12% dividend. The Series J Preferred Stock represents 984,971 shares distributed to Geneve on the date of the closing of the Merger and 10,000,000 shares received by Nasco Holdings as part of the exchange for its shares of Nasco's Common Stock.. 7,909

Total...	$8,534

Dividends are subject to the discretion of the Aristotle Board of Directors and will be affected in part by future financial performance, available cash and restrictions on cash dividends as set forth in credit agreements which have been entered into by Nasco and assumed by Aristotle.

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THE ARISTOTLE CORPORATION
PRO FORMA BALANCE SHEET
AS OF DECEMBER 31, 2001
(DOLLARS IN THOUSANDS)
(UNAUDITED)

	Nasco Historical	Aristotle Historical	Recapitalization of Nasco	Purc of Ar
Cash and cash equivalents..................	$4,465	$4,388	$ --	
Marketable securities......................	--	794	--	
Accounts receivable........................	13,750	716	--	(
Inventories................................	24,326	847	--	
Deferred income taxes......................	1,176	--	--	5,
Other current assets.......................	6,275	154	--	
Total current assets.......................	49,992	6,899	--	6,
Property, plant and equipment, net.........	9,561	1,544	--	(1,
Other assets:				
Goodwill-net...............................	7,346	6,768	--	(6,
Deferred income taxes......................	423	--	--	27
Other noncurrent assets....................	114	529	--	(
	$67,436	$15,740	$ --	$25

Current maturities of long-term debt.......	$8,403	$85	$ --	$
Accounts payable..........................	3,694	497	--	
Accrued expenses..........................	5,385	482	150(1)	1,
Accrued tax reserves......................	--	720	--	
Deferred revenue..........................	--	73	--	
Total current liabilities.................	17,482	1,857	150	1
Long-term debt............................	36,027	659	--	
Total liabilities.........................	53,509	2,516	150	1
Common stock..............................	--	20	150(1)	
Additional paid-in capital................	3,253	163,904	(60,150)(1)	(160
Preferred stock--Series I.................	--	--	--	5
Preferred stock--Series J.................	--	--	59,850(1)	5
Retained earnings (deficit)...............	10,872	(150,541)	--	172
Treasury stock............................	--	(69)	--	
Foreign currency translation..............	(198)	16	--	
Net unrealized investment losses..........	--	(106)	--	
Total stockholders' equity................	13,927	13,224	(150)	23
	$67,436	$15,740	$ --	$25

FOOTNOTES TO PRO FORMA BALANCE SHEET
AS OF DECEMBER 31, 2001
(DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)
(UNAUDITED)

(1)(a) The issuance of fifteen million shares of common stock to Nasco Holdings:

Number of shares......................................	15,000,000
Common stock ($.01 par value).........................	$150
Paid-in-capital.......................................	(150)

(b) The issuance of ten million shares of Series J preferred stock to Nasco Holdings:

Number of shares......................................	10,000,000
Preferred stock ($6.00 stated value per share)...........	$60,000
Preferred stock--estimated future cost of registration...	(150)
Preferred stock--net..................................	59,850
Accrued expenses--estimated future cost of registration..	150
Paid-in-capital.......................................	(60,000)

(2) The timing of payments between Nasco and Aristotle.

(3) Elimination of intercompany transactions between Nasco and Aristotle.

(4)

The fair market value purchase price adjustment of Aristotle inventory......	$631
The elimination of intercompany transactions between Nasco and Aristotle....	28
Total..	$659

(5)(a) The current portion of the total net deferred tax asset of $33,184 related to the expected future utilization of Aristotle's federal net operating loss carryforwards, or NOLs. Aristotle's historical financial statements reflected a full valuation allowance related to its NOLs as a result of uncertainties regarding the realization of assets, including the lack of predictability of Aristotle's profitability and the variability of its operating results. However, as a result of projected future operating results of the combined entities, NOLs of $94,800 are expected to be utilized to offset federal taxable income through 2006 and a portion of 2007. Accordingly, a net deferred tax asset of $33,184, reflecting a 35% federal tax rate, has been recognized as an asset when recording the fair market value of assets and liabilities acquired. Aristotle NOLs which are projected to expire unutilized at the end of 2006 are included in the valuation allowance and, therefore, are not recognized as an asset... $5,817

(b) The deferred tax liability resulting principally from the fair value adjustment of Aristotle's inventory....................... (232)

Total...	$5,585

(6) The recognition of the deferred tax asset related to the expected future utilization of Aristotle's net operating loss carryforwards will result in the elimination of Aristotle's long-term assets and the creation of negative goodwill. The long-term assets eliminated are $6,768 of goodwill, $1,544 of property, plant, and equipment, and $529 of other long-term assets.

(7)(a) The non-current portion of the total net deferred tax asset of $33,184 related to the expected future utilization of Aristotle's federal NOLs... $27,367

(b) The deferred tax asset resulting principally from the difference between the carrying value of property, plant and equipment for accounting and tax purposes.. 539

Total..	$27,906

(8) Elimination of intercompany transactions between Nasco and Aristotle.

(9) Estimated transaction costs to be incurred in connection with the Merger.

(10)(a) The value of common stock issued to non-Geneve shareholders at fair market value:

Number of shares...................	946,610
Price per share....................	$2.95
Total value........................	$2,792
Common stock ($.01 par value)......	$9

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Paid-in-capital...................	$2,783

(b) The value of Common Stock issued to Geneve at historical carryover basis:

Number of shares.....................	984,971
Average weighted cost per share	$5.91
Total value..........................	$5,817

Common stock ($.01 par value).........	$10
Paid-in-capital......................	$5,807

The cost per share used in the adjustment is based on the historical cost of such shares adjusted to reflect the applicable equity income and loss of Aristotle but unadjusted for the subsequent Series I dividend.

(c) The value of the 115,500 stock options included in Aristotle's 1997 Stock Plan and 80,000 stock appreciation rights, or SARs, included in Aristotle employment agreements. Aristotle has computed the value of each stock option at $3.66 using the Black-Scholes option-pricing model and the value of each SAR at $1.95, which is equivalent to the excess of the assumed fair market value over the stated price. All 1997 Stock Plan options are fully vested.

Paid-in-capital...............................	$579

(d) The elimination of Aristotle's common stock and paid-in-capital:

Common stock....	$20
Paid-in-capital....	$163,904

(e) The offset to the Series J Preferred Stock issued to Geneve in conjunction with the Merger:

Number of shares..........................	984,971
Stated value per share.....................	$6.00
Reduction in paid-in-capital................	$5,910

(11) The Series I Preferred Stock issued to non-Geneve stockholders in conjunction with the Merger:

Number of shares	946,610
Stated value per share.....................	$6.00
Total value...............................	$5,680

(12) The Series J Preferred Stock issued to Geneve in conjunction with the Merger:

Number of shares	984,971
Stated value per share.....................	$6.00
Total value...	$5,910

(13)(a)	The extraordinary gain related to the negative goodwill created by the Merger:	
	Purchase price..	$14,868
	Transaction costs incurred..	1,198
	Total purchase price..	16,066
	Value of net assets acquired (The net assets acquired are principally comprised of the historical net assets of Aristotle of $13,224 and the total net deferred tax asset of $33,184 related to the expected future utilization of Aristotle's federal net operating loss carry forwards)..	(47,346)
	Elimination of Aristotle long term assets...........................	8,841
	Excess of the value of net assets acquired over the purchase price (negative goodwill)...	22,439
(b)	The elimination of Aristotle's historical retained deficit...........	150,541
(c)	The elimination of intercompany transactions between Nasco and Aristotle..	(102)
	Total..	$172,878

(14) The elimination of Aristotle's historical treasury stock.

(15) The elimination of Aristotle's historical foreign currency translation gains.

(16) The elimination of Aristotle's historical unrealized investment losses.

3. RECENT ACCOUNTING PRONOUNCEMENTS

The Company adopted the provisions of Statement of Financial Accounting Standards No. 141, BUSINESS COMBINATIONS ("SFAS 141") as of July 1, 2001. SFAS 141 requires that the purchase method of accounting be used for all business combinations. SFAS 141 specifies criteria that intangible assets acquired in a business combination must meet to be recognized and reported separately from goodwill. The Company adopted the provisions of SFAS No. 142, GOODWILL AND OTHER INTANGIBLE ASSETS ("SFAS 142") effective January 1, 2002. Under SFAS 142, goodwill is no longer subject to amortization over its estimated useful life. Instead, SFAS 142 requires that goodwill be evaluated at least annually for impairment by applying a fair value based test and, if impairment occurs, the amount of impaired goodwill must be written off immediately. The Company evaluated its goodwill at June 30, 2002, and determined that no impairment of goodwill existed.

For the three and six months ended June 30, 2002 and 2001, a reconciliation of reported net earnings to adjusted net earnings before amortization of goodwill is as follows (dollars in thousands, except per share data):

	Three Months Ended June 30,	
	2002	2001
Net income applicable to common shareholders before extraordinary gain	$2,520	$2,189
Amortization of goodwill	-	136
Adjusted net earnings	$2,520	$2,325

Basic and diluted earnings per common share:		
Net earnings as reported before extraordinary gain	$ .16	$ .15
Amortization of goodwill	--	.01
Adjusted net earnings	$ .16	$ .16

In August 2001, the Financial Accounting Standards Board issued SFAS 144, ACCOUNTING FOR THE IMPAIRMENT OR DISPOSAL OF LONG-LIVED ASSETS ("SFAS 144"). SFAS 144 modifies the rules for accounting for the impairment or disposal of long-lived assets. Aristotle adopted SFAS 144 on January 1, 2002. The impact of the adoption of SFAS 144 did not have a material effect on the financial statements or operations of the Company.

SFAS No. 145, RESCISSION OF FASB STATEMENTS NO. 4,44, AND 64, AMENDMENT OF FASB STATEMENT NO. 13 AND TECHNICAL CORRECTIONS ("SFAS 145") updates, clarifies and simplifies several existing accounting pronouncements. Among other things, SFAS No. 145 eliminates the requirement to aggregate gains and losses from early extinguishments of debt and, if material, to classify these as an extraordinary item, net of related income tax effect. SFAS No. 145 is not expected to have a material impact on Aristotle's consolidated financial statements.

SFAS No. 146, ACCOUNTING FOR COSTS ASSOCIATED WITH EXIT OR DISPOSAL ACTIVITIES, requires that a liability be recognized for these costs only when incurred, while existing practice calls for recognition of a liability when an entity commits to an exit plan. This statement is effective for exit or disposal activities initiated after December 31, 2002 and is not expected to have a material impact on Aristotle's consolidated financial statements.

4. ACCOUNTING FOR STOCK-BASED COMPENSATION

In June 2002, the Company adopted a change in accounting principles to adopt SFAS No.123 and recognize the fair value of stock options granted on or after January 1, 2002 as an expense on its income statement. The total fair value of the 996,000 options issued during this period was $1.5 million. This amount will be recognized as compensation expense over the 3-year vesting period for such options. The change in accounting reduced net income for the

second quarter and the first six months of 2002 by approximately $11,000. The expected annual impact on net income of the options granted in June 2002 is approximately $300,000.

5. DEBT AGREEMENTS

On September 27, 1999, Simulaids and Citizens Bank of Connecticut entered into a $2.0 million credit agreement. Simulaids' outstanding indebtedness under the credit agreement is currently comprised of an $800,000 seven-year mortgage, secured by the primary facility in which Simulaids conducts its business. Principal payments are scheduled on a fifteen-year straight-line amortization, with a balloon payment at the seven-year maturity. Interest is charged at the rate of LIBOR plus 200 basis points on a 30, 60, 90 or 180 day LIBOR rate at Simulaids' election. As of June 30, 2002, the balance outstanding on the mortgage was $649,000. Future principal payments on the mortgage are $5,000 per month until September 2006, at which time the remaining balance will be due.

On May 29, 2001, Nasco and its primary lenders entered into a $51.0 million 5-year credit agreement ("5-Year Credit Agreement"). Proceeds from the credit agreement were used to extinguish $29.0 million of existing debt with its prior lenders, to complete the acquisitions of AMEP and Spectrum, to retire a $2.5 million note payable to its parent, and to extinguish $2.5 million of existing American Educational Products, LLC ("AMEP) bank debt. The 5-Year Credit Agreement had an outstanding balance of $44.0 million at June 30, 2002. The terms of the 5-Year Credit Agreement require a reduction in the principal outstanding of $4.0 million by September 30, 2002 and $4.0 million by December 31, 2002. At June 30, 2002, the weighted average interest rate on the $44.0 million principal balance is 4.2%, fixed through the end of September 2002. Interest is charged at the rate of LIBOR plus 187.5 basis points on a 30, 60, 90 or 180 day LIBOR rate at Nasco's election.

Also, on May 29, 2001, Nasco and its primary lenders entered into a $2.5 million 364 Day credit agreement ("364 Day Credit Agreement"). The stated maturity date of the 364 Day Credit Agreement was subsequently amended to June 28, 2002, and further extended until June 16, 2003. At June 30, 2002, there was no principal balance outstanding on the 364 Day Credit Agreement.

On June 17, 2002, the primary lenders on the Five-Year Credit Agreement and the 364 Day Credit Agreement consented to the Merger, and certain amendments thereto were made. Also on that date, following the Merger, Aristotle executed assumption agreements with the lenders, assuming the obligations under the Five-Year Credit Agreement and the 364 Day Credit Agreement, as amended. Simulaids and Safe Passage are not parties to either of the foregoing credit agreements.

6. EARNINGS PER COMMON SHARE

The following information presents the Company's computations of basic earnings per share ("basic EPS") and diluted earnings per share ("diluted EPS") for the periods presented in the consolidated statements of earnings:

(dollars in thousands, except share and per share data)

	Income (Numerator)	Shares (Denominator)
THREE MONTHS ENDED JUNE 30, 2002:		
Basic EPS:		
Income before extraordinary gain	$ 2,520	15,290,241
Extraordinary gain	20,237	15,290,241
Net income	$ 22,757	15,290,241
Diluted EPS:		
Income before extraordinary gain	$ 2,520	15,518,106*
Extraordinary gain	20,237	15,518,106*
Net income	$ 22,757	15,518,106*

* Includes the dilutive effect of 996,000 employee stock options.

THREE MONTHS ENDED JUNE 30, 2001:		
Basic and diluted EPS	$ 2,189	15,000,000
SIX MONTHS ENDED JUNE 30, 2002:		
Basic EPS:		
Income before extraordinary gain	$ 3,972	15,145,922
Extraordinary gain	20,237	15,145,922

Net income	$ 24,209	15,145,922
	=========	
Diluted EPS:		
Income before extraordinary gain	$ 3,972	15,373,787*
Extraordinary gain	20,237	15,373,787*

Net income	$ 24,209	15,373,787*
	=========	

* Includes the dilutive effect of 996,000 employee stock options

SIX MONTHS ENDED JUNE 30, 2001:		
Basic and diluted EPS	$ 2,935	15,000,000

7. COMPREHENSIVE INCOME

Comprehensive income requires disclosure of total comprehensive income (net income plus changes in equity that result from transactions and economic events from non-owner sources). Comprehensive income for the three and six months ended June 30, 2002 and 2001 is as follows ($000 omitted):

	Three Months Ended June 30,	
	2002	2001
Net income applicable to common shareholders	$22,757	$2,189
Foreign currency translation adjustment	(17)	(2)
Net unrealized investment gain	14	--
	-------	------
Comprehensive income	$22,754	$2,187
	=======	======

8. SEGMENT REPORTING

Aristotle's business activities are organized into two principal business segments, Educational and Commercial. The Educational segment markets instructional teaching aids and materials to educational institutions nationwide, primarily kindergarten through grade 12 classes. The primary marketing tool is the publication and distribution of catalogs containing a selection of over 80,000 items to these institutions. The catalogs carry the branding of Nasco, Triarco, Summitt Learning, Hubbard Scientific, Scott Resources and Spectrum Educational Supplies. In addition, Aristotle, through Nasco and its subsidiary, Simulaids, offers simulation kits and manikins used for training in cardiopulmonary resuscitation and in the fire and emergency rescue and patient care fields. Potential for this segment to grow is directly related to school enrollments and the relative strength of government funding of education. The Commercial segment is comprised of several commercial industries, including agriculture, food, sterile sampling containers and systems, senior care activities, and novelty and gift products. This segment markets its products through catalog distribution nationwide and through a worldwide dealer network representing more than 60 countries. Market growth in this segment is related to the general economic conditions of world agriculture, the increasing size of aged population, as well as increasing global awareness of food and water quality standards. Aristotle evaluates the performance of these segments based on segment sales and gross profit.

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The following table presents segment information for the three and six months ended June 30, 2002 and 2001 ($000 omitted):

	Three Months Ended June 30		Six Month
	2002	2001	2002
Net Sales:			
Educational	$35,974	$35,736	$63,235
Commercial	7,869	7,915	15,385
Intercompany/other	(521)	(413)	(769)
Net Sales	$43,322	$43,238	$77,851
Gross Profit:			
Educational	$13,945	$13,445	$24,718
Commercial	2,937	2,734	5,617
Other cost of sales	(1,547)	(1,368)	(2,748)
Gross Profit	$15,335	$14,811	$27,587

	June 30, 2002	December 31, 2001
Identifiable assets:		
Educational	$ 27,939	$25,056
Commercial	5,746	3,937
Other corporate assets	84,940	38,443
Identifiable assets	$118,625	$67,436

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

GENERAL

This discussion and analysis of financial condition and results of operations reviews the results of operations of Aristotle (after giving effect to the Merger), on a consolidated basis, for the three and six months ended June 30, 2002, as compared to the three and six months ended June 30, 2001. This discussion and analysis of financial condition and results of operations have been derived from, and should be read in conjunction with, the unaudited Consolidated Financial Statements and Notes to Consolidated Financial Statements contained herein.

We believe the following accounting policies affect the more significant judgments and estimates used in the preparation of our consolidated financial statements.

Revenues - Customarily applying FOB-shipping point terms, Aristotle recognizes revenue upon shipment of products to its customer, which corresponds to the time when risk of ownership transfers. The point of shipment may be from one of Aristotle's distribution centers or from a vendor's location as a drop shipment. All drop shipment sales are recorded at gross selling price. An allowance is provided for estimated future returns.

Goodwill - Aristotle adopted "SFAS 141" as of July 1, 2001. SFAS 141 requires that the purchase method of accounting be used for all business combinations. SFAS 141 specifies criteria that intangible assets acquired in a business combination must meet to be recognized and reported separately from goodwill. Aristotle also adopted the provisions of SFAS No. 142, effective January 1, 2002. Under SFAS 142, goodwill is no longer subject to amortization over its estimated useful life. Instead, SFAS 142 requires that goodwill be evaluated at least annually for impairment by applying a fair value based test and, if impairment occurs, the amount of impaired goodwill must be written off immediately. Aristotle evaluated its goodwill at June 30, 2002, and determined that no impairment of goodwill existed.

Taxes - The June 30, 2002 balance sheet contains a deferred tax asset of approximately $30 million related to Aristotle's federal tax net operating loss carryforwards. This asset is expected to be utilized to offset future federal taxable income through 2006 and a portion of 2007. The realizability of this asset is dependent upon projected future operating results and Aristotle's ability to retain its net operating tax loss carryforward position. The asset recognized at June 30, 2002 is net of a valuation allowance of approximately $12 million, which is subject to future adjustment based upon changes in management's evaluation of the realizability of the deferred tax asset.

RESULTS OF OPERATIONS FOR THE COMPANY

FOR THE THREE MONTHS ENDED JUNE 30, 2002 AS COMPARED TO THE THREE MONTHS ENDED JUNE 30, 2001.

Net sales for the three months ended June 30, 2002 increased 0.2% to $43.3 million compared to net sales of $43.2 million for the prior year. Net sales in the Educational segment, totaling $36.0 million in the second quarter of 2002, increased 0.7% compared to the second quarter of 2001. The Commercial segment recorded net sales of $7.9 million in the second quarter of 2002, decreasing 0.6%. The lack of sales growth in the second quarter reflects the downturn in the U.S. economy and the related budget constraints in the U.S. education sector.

Gross profit for the three months ended June 30, 2002 increased 3.5% to $15.3 million from $14.8 million in the same period last year. The gross profit margin percentage improved to 35.4% in the second quarter of 2002 compared to the prior year gross profit margin of 34.3%. The Educational segment yielded a gross profit margin of 38.8% in the second quarter of 2002, improving on the 2001 gross profit margin of 37.6%. The Commercial segment gross profit margin was 37.3% compared to 34.5% for the second quarter of 2001. Building upon efforts initiated in the first quarter of 2002, the Company improved its second quarter gross profit margins through purchasing efforts to reduce merchandise costs.

Selling, general and administrative expenses for the quarter ended June 30, 2002 were $10.0 million as compared to $9.9 million in 2001, remaining virtually even with the same period last year. Selling, general and administrative expenses at AMEP, a

wholly- owned limited liability company of Aristotle, were reduced $0.7 million compared to the second quarter of 2001 through consolidation of distribution services and implementation of other operating efficiencies.

In addition, in the three months ended June 30, 2001, selling, general and administrative expenses included goodwill amortization of $136,000. As discussed above, effective January 1, 2002, Aristotle adopted SFAS No. 142 and no longer amortizes goodwill as a reduction to earnings from operations.

During the second quarter of 2001 and not recurring in 2002, AMEP incurred certain costs classified as special charges in the accompanying Condensed Consolidated Statements of Operations. These non-recurring costs include $516,000 of various legal, accounting and regulatory fees incurred by AMEP in connection with Aristotle's acquisition of AMEP.

Interest expense decreased to $0.5 million in the three months ended June 30, 2002 compared to $0.8 million in the prior period. The decrease reflects the variance in interest rates in effect. The applicable interest rates assessed under Aristotle's various credit agreements, averaged 4.5% in the second quarter of 2002, compared to 6.7% in the second quarter of 2001. The applicable interest rate for the long-term debt has been fixed at rates that average 4.5% through September 2002. The principal balance outstanding under these credit agreements amounted to $44.8 million and $49.0 million at June 30, 2002 and 2001, respectively.

The income tax provision for the three months ended June 30, 2002 was $1.9 million compared to $1.4 million for the three months ended June 30, 2001. The difference between the Federal statutory income tax rate of 35% and the effective income tax rate results principally from state income taxes. The balance sheet contains a deferred tax asset at June 30, 2002 of approximately $30 million related to Aristotle's federal net operating tax loss carryforwards. The utilization of this asset to offset future federal taxable income will result in Aristotle not having to pay federal income taxes for approximately the next five years.

Preferred stock dividends of $0.3 million were accrued during the three months ended June 30, 2002. This amount represents dividends on 1,046,716 shares of Series I Preferred Stock and 10,984,971 shares of Series J Preferred Stock for the period June 18, 2002 to June 30, 2002. There was no preferred stock outstanding in the period ended June 30, 2001.

An extraordinary gain of $20.2 million was recognized during the three months ended June 30, 2002 which represented the negative goodwill arising principally from the deferred tax benefits recognized at the date of the Nasco merger.

FOR THE SIX MONTHS ENDED JUNE 30, 2002 AS COMPARED TO THE SIX MONTHS ENDED JUNE 30, 2001.

Net sales for the six months ended June 30, 2002 increased 2.1% to $77.9 million compared to net sales of $76.2 million for the prior year. The growth in net sales is positively impacted by the acquisition of Spectrum Educational Supplies, Ltd., ("Spectrum") completed in April 2001. Spectrum has contributed $3.9 million in net sales in the first six months of 2002, compared to $2.1 million from the acquisition date to June 30, 2001. Excluding the net sales from Spectrum, net sales declined 0.2% in the six months of 2002 compared to the same period of 2001.

Net sales in the Educational segment, totaling $63.2 million, increased 3.1% in the first six months of 2002 compared to 2001. Excluding the sales realized from Spectrum, the Educational segment sales increased 0.2% from 2001. The Commercial segment recorded net sales of $15.4 million in the first six months of 2002, decreasing 1.0% versus the prior year. The lack of growth in year to date sales reflects the downturn in the U.S. economy as well as budgetary uncertainty in the U.S. education sector.

Gross profit for the six months ended June 30, 2002 increased 5.9% to $27.6 million from $26.1 million in the same period last year. The gross profit margin percentage improved to 35.4% in the first six months of 2002 compared to the prior year gross profit margin of 34.2%. Spectrum produced $1.8 million in gross profit in the first six months of 2002, compared to $0.8 million in the first six months of 2001. Excluding the gross profit realized from Spectrum, the gross profit margin would still be 34.9% for the six months ended June 30, 2002, compared to 34.1% for the same period last year. The Educational segment yielded a gross profit margin of 39.1% in the six months of 2002, improving on the 2001 gross profit margin of 37.7%. Excluding the Spectrum gross profit, the 2002 Educational segment gross profit margin would be 38.6%, compared to 37.7% in 2001. The Commercial segment gross profit margin was 36.5% compared to 35.0% for the first six months of 2001. In general, Aristotle improved its gross profit margins for the first six months of 2002 through purchasing efforts to reduce merchandise costs implemented throughout the period.

Selling, general and administrative expenses for the six months ended June 30, 2002 were $19.5 million as compared to $19.2 million in 2001, increasing 1.6% compared to the same period last year. Excluding Spectrum, selling, general and administrative expense decreased by $0.2 million, or 1.0%. Selling, general and administrative expenses at AMEP, were reduced $1.6 million compared to the first six months of 2001 through consolidation of distribution services and implementation of other operating efficiencies.

In the six months ended June 30, 2001, selling, general and administrative expenses included goodwill amortization of $202,000. As discussed above, effective January 1, 2002, Aristotle adopted SFAS No. 142 and no longer amortizes goodwill as a reduction to earnings from operations.

During the first six months of 2001 and not recurring in 2002, AMEP incurred certain costs classified as special charges in the accompanying Condensed Consolidated Statements of Earnings. These non-recurring costs include $567,000 of various legal, accounting and regulatory fees incurred by AMEP in connection with Aristotle's acquisition of AMEP. The special charges are reported as a reduction to earnings from operations.

Interest expense decreased to $1.0 million in the six months ended June 30, 2002 compared to $1.6 million in the prior period. The decrease reflects the variance of interest rates in effect in 2002 compared to 2001. The applicable interest rates assessed by Aristotle's various credit agreements averaged 4.3% in the first six months of 2002, compared to 7.5% in the first six months of 2001. The applicable interest rate for the long-term debt has been fixed at rates that average 4.5% through September 2002. The principal balance outstanding under these credit agreements amounted to $44.8 million and $49.0 million at June 30, 2002 and 2001, respectively.

The income tax provision for the six months ended June 30, 2002 was $2.8 million compared to $1.8 million for the six months ended June 30, 2001. The difference between the Federal statutory income tax rate of 35% and the effective income tax rate results principally from state income taxes. The balance sheet contains a deferred tax asset at June 30, 2002 of approximately $30 million related to Aristotle's federal net operating tax loss carryforwards. The utilization of this asset to offset future federal taxable income will result in Aristotle not having to pay federal income taxes for approximately the next five years.

Preferred Stock dividends of $0.3 million were accrued during the six months ended June 30, 2002. This amount represents dividends on 1,046,716 shares of Series I Preferred Stock and 10,984,971 shares of Series J Preferred Stock for the period June 18, 2002 to June 30, 2002. There was no preferred stock outstanding in the period ended June 30, 2001.

An extraordinary gain of $20.2 million was recognized during the six months ended June 30, 2002 which represented the negative goodwill arising principally from the deferred tax benefits recognized at the date of the Merger.

LIQUIDITY AND CAPITAL RESOURCES

At June 30, 2002, Aristotle had cash and cash equivalents of $9.1 million compared to $4.5 million at December 31, 2001. The overall change in cash and cash equivalents of $4.6 million is detailed below.

Aristotle generated $2.5 million of cash from operations during the six months ended June 30, 2002. During this period, Aristotle generated cash from earnings plus noncash income and deductions of $4.9 million, an increase in prepaid expenses, primarily advertising costs of $0.6 million, an increase of $7.8 million in trade accounts payable, and an increase of $1.7 million in accrued expenses. Offsetting these items, trade accounts receivable increased by $4.8 million, and inventories increased by $8.0 million. These changes in current assets and liabilities are typical for this quarter as Aristotle enters its peak business cycle in the summer months. Aristotle used $0.1 million of cash for operations during the six months ended June 30, 2001. During this period, Aristotle generated cash from earnings plus depreciation and amortization of $4.0 million, an increase in prepaid expenses, primarily advertising costs, of $0.8 million, an increase of $8.1 million in trade accounts payable, and an increase of $3.0 million in accrued expenses. Offsetting these items, trade accounts receivable increased by $6.3 million, and inventories increased by $9.7 million. These changes in current assets and liabilities are typical for this quarter as Aristotle enters its peak business cycle in the summer months.

Aristotle generated $2.5 million of cash from investing activities during the six months ended June 30, 2002. Aristotle invested $0.8 million in capital expenditure purchases to replace and upgrade existing capital equipment and install new equipment and fixtures in order to provide additional operating capacity and efficiency. As a result of the Merger, cash increased by $3.3 million. Aristotle used $11.0 million of cash in investing activities in the six months ended June 30, 2001. The investing activity included $5.2 million paid to the minority shareholders of AMEP for their minority ownership interests, and $5.0 million for the acquisition of the ownership interests in Spectrum. During that period, Aristotle invested $0.8 million in capital expenditure purchases to replace and upgrade existing capital equipment and install new equipment and fixtures in order to provide additional operating capacity and efficiency.

During the six months ended June 30, 2002, Aristotle used cash of $0.4 million in financing activities. The debt payments were to service existing capital leases and other seller notes payable by AMEP incurred in previous acquisitions. As of June 30, 2002, the balance outstanding under its credit agreements was $44.8 million. Aristotle remained in compliance with all terms and conditions of its primary credit agreement throughout this period. During the six months ended June 30, 2001, financing activities provided cash of $11.9 million. Aristotle borrowed $20.0 million under an amended credit agreement with its lenders. The funds were used to retire AMEP's short-term debt of $2.5 million, and to retire $5.4 million of short-term debt to Geneve Corporation related to the 2000 fiscal year transfer of the AMEP ownership interest as well as the Spectrum and AMEP acquisitions. Aristotle also used $0.4 million to retire debt in accordance with the terms of its capital lease commitments. Aristotle remained in compliance with all terms and conditions of its credit agreements throughout this period.

Aristotle's cash obligations as of June 30, 2002 are as follows (in thousands):

Contractual Obligations	Total Amounts Committed	2002	2003 and 2004
Principal portion of long-term credit facility	$44,000	$8,000	$18,000
Principal portion of mortgage debt	649	54	107
Principal portion of capital lease obligations	111	54	57
Operating lease obligations	2,356	522	1,313
Employment obligations	658	266	392
Total	$47,774	$8,896	$19,869

The long-term credit facility is the Five-Year Credit Agreement. The Five-Year Credit Agreement provides specific dates and amounts by which the size of the principal amount of its capacity is reduced, amortizing the outstanding debt through March 2006. The Credit Agreement is secured by the assets of Nasco. Interest is charged at the rate of LIBOR plus 187.5 basis points on a 30, 60, 90 or 180 day rate at election.

The mortgage debt consists of the financing agreement between Simulaids and its primary lender used to finance land and buildings located in Woodstock, New York. Principal payments are scheduled on a fifteen-year straight-line amortization, with a balloon payment in September 2006. Interest is charged at the rate of LIBOR plus 200 basis points on a 30, 60, 90 or 180-day LIBOR rate at Simulaids' election.

The capital lease obligations, related to computer equipment at Simulaids and AMEP, consist of arrangements with IBM Credit Corporation and another leasing company. The lease terms require monthly payments until September 2003 and January 2004, respectively. The capital leases bear annual interest rates in the range of 8.5% to 11.5%.

Aristotle, through its Nasco division, leases office and distribution facilities in Plymouth, Minnesota, Fort Atkinson, Wisconsin, Chippewa Falls, Wisconsin, and Aurora, Ontario, Canada. The terms and conditions of the leases vary by location, generally falling within terms and conditions which are "market" for the respective locations in which Aristotle operates. Current lease terms expire in 2003 through 2006. Aristotle leases its office facility in New Haven, Connecticut, which expires in 2002. Safe Passage leases its office facility in Rochester, New York, which expires in 2002.

The employment obligations consist of written agreements with John J. Crawford and Paul M. McDonald of Aristotle and James S. Viscardi and Michael R. Rooksby of Safe Passage.

Capital resources in the future are expected to be used to retire long term debt, invest in additional capital projects designed to enhance operating efficiencies and to acquire additional companies. The balance sheet contains a deferred tax asset at June 30, 2002 of approximately $30 million related to Aristotle's federal net operating tax loss carryforwards. The utilization of this asset to offset future federal income taxable income will result in Aristotle not having to pay federal taxes for approximately the next five years.

Aristotle anticipates that there will be sufficient financial resources to meet its projected working capital and other cash requirements for at least the next twelve months.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

As described below, credit risk and interest rate risk are the primary sources of market risk to Aristotle in its marketable securities and long-term borrowings.

QUANTITATIVE

Aristotle's marketable securities and long-term borrowings as of June 30, 2002 are as follows (in thousands):

	Maturity less than one year	Maturity greater than one year
Marketable securities		
Cost basis	$ --	$ 834
Weighted average return	--	6.6%
Fair market value	$ --	$ 848
Long-term borrowings		

Amount	$ 8,128	$ 36,631
Weighted average interest rate	4.5%	4.5%
Fair market value	$ 8,128	$ 36,631

QUALITATIVE

Interest Rate Risk: Changes in interest rates can potentially impact Aristotle's profitability and its ability to realize assets and satisfy liabilities. Interest rate risk is resident primarily in Aristotle's marketable securities and long-term borrowings, which have fixed coupon or interest rates.

Credit Risk: Aristotle's marketable securities are invested in investment grade corporate bonds and closed-end bond funds, both domestic and international, which have various maturities.

CERTAIN FACTORS THAT MAY AFFECT FUTURE RESULTS OF OPERATIONS

Aristotle believes that this report may contain forward-looking statements within the meaning of the "safe-harbor" provisions of the Private Securities Litigation Reform Act of 1995. These forward-looking statements include statements regarding Aristotle's liquidity and are based on management's current expectations and are subject to a number of factors and uncertainties that could cause actual results to differ materially from those described in the forward-looking statements. Aristotle cautions investors that there can be no assurance that actual results or business conditions will not differ materially from those projected or suggested in such forward-looking statements as a result of various factors including, but not limited to, the following: (i) the ability of Aristotle to obtain financing and additional capital to fund its business strategy on acceptable terms, if at all; (ii) the ability of Aristotle on a timely basis to find, prudently negotiate and consummate additional acquisitions; (iii) Aristotle's ability to manage Nasco, Simulaids, Safe Passage and any other acquired or to be acquired companies; (iv) the ability of Aristotle to retain and utilize its tax net operating loss carryforward position; and (v) general economic conditions. As a result, the Company's future development efforts and operations involve a high degree of risk. For further information, please see Aristotle's filings with the Securities and Exchange Commission, including its Forms 10-K and 10-Q.

PART II - OTHER INFORMATION

ITEM 1 - LEGAL PROCEEDINGS.

None.

ITEM 2 - CHANGES IN SECURITIES.

(a) On June 17, 2002, Aristotle consummated the merger (the "Merger") with Nasco International, Inc. ("Nasco") contemplated by that certain Agreement and Plan of Merger dated as of November 27, 2001, as amended (the "Merger Agreement"). Pursuant to the terms of the Merger Agreement, as of June 17, 2002, the separate corporate existence of Nasco ceased and Aristotle was the surviving entity. Due to the relative sizes of the parties to the Merger, the transaction was accounted for as a reverse acquisition using the purchase method of accounting under generally accepted accounting principles.

As consideration for the Merger, the sole shareholder of Nasco received 15,000,000 shares of Aristotle's common stock and 10,000,000 shares of Aristotle's newly authorized Series J $6.00 non-convertible, non-voting, cumulative 12% preferred stock, par value $0.01 per share ("Series J Preferred Stock"). Separately, Aristotle's Board of Directors declared, and Aristotle paid, a stock dividend on each share of Aristotle's common stock outstanding of one share of newly authorized Series I $6.00 convertible, voting, cumulative 11% preferred stock, par value $0.01 per share ("Series I Preferred Stock").

See the following sections of Aristotle's Proxy Statement-Prospectus, dated May 15, 2002, contained in Aristotle's Registration Statement on Form S-4 (File No. 333-86026) filed with the Securities and Exchange Commission on April 11, 2002 (the "Proxy Statement-Prospectus") for a detailed discussion of Aristotle's Amended and Restated Certificate of Incorporation and Second Amended and Restated Certificate of Incorporation and the effect of such modifications on the rights of the holders of Aristotle's common stock, Series I Preferred Stock and Series J Preferred Stock: "Changes to Aristotle's Certificate of Incorporation" and "Description of Aristotle's Capital Stock". The information contained in the foregoing noted sections of the Proxy Statement-Prospectus are incorporated herein by reference.

(b) None.

(c) In connection with the Merger, on June 17, 2002, Aristotle issued to the sole shareholder of Nasco, among other things, 10,000,000 shares of its Series J Preferred Stock. In addition, Aristotle issued 984,971 shares of Series J Preferred Stock to Geneve as a stock dividend. The shares of Series J Preferred Stock issued were not registered under the Securities Act of 1933, as amended. The shares of Series J Preferred Stock were issued in partial consideration for the shares of Nasco held by the sole shareholder and as a stock dividend on the shares of Aristotle's common stock held by Geneve.

See the following sections of Aristotle's Proxy Statement-Prospectus which are incorporated herein by reference, for the information required by Item 701 of Regulation S-K: "Restrictions on Sales of Shares of Aristotle Stock received by Nasco Holdings" and "Description of Aristotle's Capital Stock".

(d) None.

ITEM 3 - DEFAULTS UPON SENIOR SECURITIES.

None

ITEM 4 - SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDER.

(a) On June 17, 2002 Aristotle held its annual meeting of stockholders.

(b) At the annual meeting of stockholders, Edward Netter, John J. Crawford and Sharon M. Oster were elected as directors. The other members of the board of directors whose term of office continued after the meeting were Robert Fiscus, Betsy Henley-Cohn, John C. Warfel, Steven B. Lapin, Daniel J. Miglio and John Lahey. Following the Merger, the Board of Directors of Aristotle was comprised of the following individuals: John J. Crawford, John Lahey, Steven B. Lapin, Donald T. Netter, Edward Netter, Sharon M. Oster, James G. Tatum and Roy T. K. Thung.

See the following sections of Aristotle's Proxy Statement-Prospectus (which are incorporated herein by reference): "Operations After the Merger" and "Management of Aristotle Following the Merger-Board of Directors of Aristotle".

(c) The following matters were voted upon at the annual meeting of the stockholders of Aristotle held on June 17, 2002:

(i) A proposal to consider and vote upon the approval of the Merger Agreement among Aristotle, Geneve Corporation, Nasco Holdings, Inc. and Nasco International, Inc. This proposal was adopted by the stockholders by the following vote:

Votes cast for this proposal	1,375,538
Votes cast against this proposal	2,189
Abstentions	1,006
Broker Non-votes	407,062

(ii) A proposal to amend and restate Aristotle's certificate of incorporation, so as to authorize additional shares of Aristotle's common stock, and to authorize and set forth the rights of Aristotle's Series I Preferred Stock and Series J Preferred Stock. This proposal was adopted by the stockholders by the following vote:

Votes cast for this proposal	1,374,630
Votes cast against this proposal	3,328
Abstentions	775
Broker Non-votes	407,062

(iii) A proposal to include, as part of the amendment and restatement of Aristotle's certificate of incorporation, provisions requiring Aristotle to indemnify its directors, officers and agents and specifying procedures with respect thereto. This proposal was adopted by the stockholders by the following vote:

Votes cast for this proposal	1,370,564
Votes cast against this proposal	6,228
Abstentions	1,941
Broker Non-votes	407,062

(iv) A proposal to further amend and restate Aristotle's certificate of incorporation upon the completion of the Merger with Nasco in order to eliminate certain provisions that (A) establish staggered terms for and classification of the members of Aristotle's board of directors, (B) mandate that special meetings of Aristotle's stockholders may only be called by the chairman of Aristotle's board of directors, president or board of directors, (C) state that any action required or permitted to be taken by Aristotle's stockholders must be taken at an annual or special meeting of the stockholders and (D) limit the manner in which Aristotle may adopt, amend or repeal its certificate of incorporation and By-laws. This proposal was adopted by the stockholders by the following vote:

Votes cast for this proposal	1,373,530
Votes cast against this proposal	3,592
Abstentions	1,611
Broker Non-votes	407,062

(v) A proposal to adopt The Aristotle Corporation 2002 Employee, Director and Consultant Stock Plan. This proposal was adopted by the stockholders by the following vote:

Votes cast for this proposal	1,368,177
Votes cast against this proposal	8,166
Abstentions	2,390
Broker Non-votes	407,062

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(vi) A proposal to elect John J. Crawford, Edward Netter and Sharon M. Oster for three year terms and until their successors are duly elected and qualified. Each nominee was elected to the board of directors by the following vote:

John J. Crawford

Votes cast for election	1,769,111
Votes withheld	16,684

Edward Netter

Votes cast for election	1,769,111
Votes withheld	16,684

Sharon Oster

Votes cast for election	1,769,111
Votes withheld	16,684

ITEM 5 - OTHER INFORMATION.

On April 11, 2002, Aristotle reached a settlement with the Internal Revenue Service regarding a refund that it had received in 1997 for a net operating loss carryback claim relating to its 1996 tax year. As previously reported, the IRS had been reviewing the amount of the refund, and Aristotle recorded a tax reserve of $720,000 with respect to such refund. In the settlement, Aristotle agreed to pay approximately $682,000 (net of the amount due from a previously paid contingency fee), plus approximately $318,000 (net of the amount due from a previously paid contingency fee), which represents interest on the portion of the unallowed refund claim.

ITEM 6 - EXHIBITS AND REPORTS ON FORM 8-K.

(a) Exhibits

Exhibit 2.5--Amendment to Agreement and Plan of Merger, dated May 7, 2002, among The Aristotle Corporation, Geneve Corporation, Nasco Holdings, Inc. and Nasco International, Inc., incorporated herein by reference to an exhibit to the Aristotle's Registration Statement on Form S-4 (File No. 333-86026).*

Exhibit 2.6--Amendment No. 2 to Agreement and Plan of Merger, dated May 15, 2002, among The Aristotle Corporation, Geneve Corporation, Nasco Holdings, Inc. and Nasco International, Inc., incorporated herein by reference to an exhibit to the Aristotle's Registration Statement on Form S-4 (File No. 333-86026).*

Exhibit 3.1--Amended and Restated Certificate of Incorporation of The Aristotle Corporation.

Exhibit 3.2--Amended and Restated Bylaws of The Aristotle Corporation.

Exhibit 4.1--Amended and Restated Certificate of Incorporation of The Aristotle Corporation and Amended and Restated Bylaws filed as Exhibits 3.1 and 3.2 are incorporated into this item by reference. See Exhibits 3.1 and 3.2 above.

Exhibit 10.1--The Aristotle Corporation 2002 Employee, Director and Consultant Stock Plan.

Exhibit 10.2--Form of Non-Qualified Stock Option Agreement (for employees, directors and consultants).

Exhibit 10.3--Form of Incentive Stock Option Agreement (for employees).

Exhibit 10.8(b)--Amendment, dated June 17, 2002, to the Employment Agreement dated as of February 1, 2001 by and between The Aristotle Corporation and Paul McDonald.

Exhibit 10.9(b)--Amendment, dated June 17, 2002, to the Employment Agreement dated as of February 1, 2001 by and between The Aristotle Corporation and John J. Crawford.

Exhibit 10.11--Letter Agreement, dated May 24, 2002, between The Aristotle Corporation and Paul McDonald regarding the exercisability of certain stock options.

Exhibit 10.12--Letter Agreement, dated May 24, 2002, between The Aristotle Corporation and John J. Crawford regarding the exercisability of certain stock options.

Exhibit 10.13--Full Recourse Promissory Note, dated June 17, 2002, made by Paul McDonald in favor of The Aristotle Corporation.

Exhibit 10.14--Form of Letter Agreement, dated May 24, 2002, between The Aristotle Corporation and non-employee directors regarding the exercisability of certain stock options.

Exhibit 10.15(b) --First Amendment to Amended and Restated Credit

Agreement (Five Year) and Consent, dated as of June 17, 2002, among Nasco International, Inc., Various Financial Institutions now or hereafter parties thereto, Bank One, Wisconsin and Bank of America, N.A.

Exhibit 10.15(c)--Assumption Agreement, dated June 17, 2002, executed by The Aristotle Corporation pursuant to Section 3.1 of the First Amendment to Amended and Restated Credit Agreement (Five Year) and Consent (See Exhibit 10.14(b)).

Exhibit 10.16(b)--Second Amendment to Amended and Restated Credit Agreement (364 Days) and Consent, dated as of June 17, 2002, among Nasco International, Inc., Various Financial Institutions now or hereafter parties thereto, Bank One, Wisconsin and Bank of America, N.A.

Exhibit 10.16(c) --Assumption Agreement, dated June 17, 2002, executed by The Aristotle Corporation pursuant to Section 3.1 of the Second Amendment to Amended and Restated Credit Agreement (364 Days) and Consent (See Exhibit 10.15(b)).

Exhibit 10.21--Assumption of Mortgage and Modification Agreement, dated as of July 12, 2002, by and between The Aristotle Corporation and Bank of America, N.A.

Exhibit 10.22--Assumption of Deed of Trust and Modification Agreement, dated as of July 12, 2002, by and between The Aristotle Corporation and Bank of America, N.A.

Exhibit 10.23--Assumption of Deed of Trust and Modification Agreement, dated as of July 12, 2002, by and between The Aristotle Corporation and Bank of America, N.A.

Exhibit 10.24--Amended and Restated Subsidiary Pledge Agreement, dated as of June 27, 2002, by and between American Educational Products LLC and Bank of America, N.A.

Exhibit 10.25--Amended and Restated Subsidiary Security Agreement, dated as of June 27, 2002, by and between American Educational Products LLC, the other subsidiaries party thereto and Bank of America, N.A.+

Exhibit 10.26--Amended and Restated Pledge Agreement, dated as of June 27, 2002, by and between The Aristotle Corporation and Bank of America, N.A.+

Exhibit 10.27--Amended and Restated Security Agreement, dated as of June 27, 2002, by and between The Aristotle Corporation and Bank of America, N.A.+

Exhibit 99.1--Registrant's Proxy Statement-Prospectus dated May 15, 2002, incorporated by reference to The Aristotle Corporation's Registration Statement on Form S-4 (File No. 333-86026).*

Exhibit 99.2--Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

* These items are hereby incorporated by reference from the exhibits of the filing or report indicated (except where noted, Commission File No. 0-14669) and are hereby incorporated by reference.

+ In accordance with Item 601(b)(2) of Regulation S-K, the schedules have been omitted and a list briefly describing the schedules is at the end of this Agreement. Aristotle will furnish supplementally a copy of any omitted schedule to the Commission upon request.

(b) Reports on Form 8-K. On April 11, 2002, The Aristotle Corporation filed a Current Report on Form 8-K under Item 5 regarding the settlement agreement with the Internal Revenue Service.

On June 19, 2002, The Aristotle Corporation filed a Current Report on Form 8-K under Items 5, 7 and 8.

On July 1, 2002, The Aristotle Corporation filed a Current Report on Form 8-K/A under Items 2 and 7.

On August 8, 2002, The Aristotle Corporation filed a Current Report on Form 8-K under Items 4 and 7.

SIGNATURES

PURSUANT TO THE REQUIREMENTS OF SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934, THE REGISTRANT HAS DULY CAUSED THIS REPORT TO BE SIGNED ON ITS BEHALF BY THE UNDERSIGNED, THEREUNTO DULY AUTHORIZED.

THE ARISTOTLE CORPORATION

/s/ John J. Crawford

John J. Crawford
ITS, CHIEF EXECUTIVE OFFICER
(PRINCIPAL EXECUTIVE OFFICER)
Date: August 14, 2002

/s/ Paul M. McDonald

Paul M. McDonald
ITS, CHIEF FINANCIAL OFFICER
(PRINCIPAL FINANCIAL AND ACCOUNTING OFFICER)
Date: August 14, 2002

EXHIBIT INDEX

Exhibit NUMBER	DESCRIPTION

2.1 - Capital Contribution Agreement dated as of November 19, 1993, by and among The Aristotle Corporation, Aristotle Sub, Inc., The Strouse, Adler Company and the Stockholders of Strouse, incorporated herein by reference to Exhibit 2.1 of The Aristotle Corporation Current Report on Form 8-K dated April 14, 1994, as amended (the "1994 Current Report").*

2.2 - Agreement and Plan of Reorganization, dated as of September 13, 2000 (closed on September 14, 2000), by and among The Aristotle Corporation, Aristotle Acquisition Sub, Inc., Safe Passage International, Inc., James S. Viscardi, Michael R. Rooksby, Howard C. Rooksby and Andrew M. Figiel, incorporated herein by reference to Exhibit 2.1 of the Registrant's Current Report on Form 8-K dated September 27, 2000.*

2.3 - Agreement and Plan of Merger, dated as of September 13, 2000 (closed on September 14, 2000), by and between Aristotle Acquisition Sub, Inc. and Safe Passage International, Inc., incorporated herein by reference to Exhibit 2.2 of the Registrant's Current Report on Form 8-K dated September 27, 2000.*

2.4 - Agreement and Plan of Merger, dated as of November 27, 2001, among The Aristotle Corporation, Geneve Corporation, Nasco Holdings, Inc. and Nasco International, Inc. incorporated herein by reference to Exhibit 2 of The Aristotle Corporation's Current Report on Form 8-K dated November 30, 2001.*

2.5 - Amendment to Agreement and Plan of Merger, dated May 7, 2002, among The Aristotle Corporation, Geneve Corporation, Nasco Holdings, Inc. and Nasco International, Inc. incorporated herein by reference to an exhibit to The Aristotle Corporation's Registration Statement on Form S-4 (File No. 333-86026).*

2.6 - Amendment No. 2 to Agreement and Plan of Merger, dated May 15, 2002, among The Aristotle Corporation, Geneve Corporation, Nasco Holdings, Inc. and Nasco International, Inc. incorporated herein by reference to an exhibit to The Aristotle Corporation's Registration Statement on Form S-4 (File No. 333-86026).*

3.1 - Amended and Restated Certificate of Incorporation of The Aristotle Corporation.

3.2 - Amended and Restated Bylaws of The Aristotle Corporation.

4.1 - Amended and Restated Certificate of Incorporation of The Aristotle Corporation and Amended and Restated Bylaws filed as Exhibits 3.1 and 3.2 are incorporated into this item by reference. See Exhibits 3.1 and 3.2 above.

4.2 - Registration Rights Agreement dated as of April 11, 1994 between The Aristotle Corporation and the shareholders listed on Exhibit A thereto, incorporated by reference to an exhibit to The Aristotle Corporation's Registration Statement on Form S-3 (File No. 333-4185).*

4.3 - Preferred Stock Purchase Agreement dated as of October 22, 1997, between The Aristotle Corporation and Geneve Corporation, incorporated herein by reference to Exhibit 10.5 of The Aristotle Corporation's Quarterly Report on Form 10-Q for fiscal quarter ended September 30, 1997.*

4.4 - Registration Rights Agreement dated as of October 22, 1997, between The Aristotle Corporation and Geneve Corporation, incorporated herein by reference to Exhibit 10.6 to The Aristotle Corporation's Quarterly Report on Form 10-Q for the fiscal quarter ended September 30, 1997.*

4.5 - Letter Agreement dated as of September 15, 1997, among The Aristotle Corporation, Aristotle Sub, Inc. and certain stockholders, incorporated herein by reference to Exhibit 10.7 to The Aristotle Corporation's Quarterly Report on Form 10-Q for the fiscal quarter ended September 30, 1997.*

4.6 - Letter Agreement dated as of February 9, 2000 between The Aristotle Corporation and the Geneve Corporation regarding certain limitations on voting and the acquisition of additional shares of common stock, incorporated herein by reference to The Aristotle Corporation's Report on Form 13D/A dated February 15, 2000.*

4.7 - Letter Agreement dated as of April 28, 2000 between The Aristotle Corporation and the Geneve Corporation, modifying the letter agreement between such parties dated as of February 9, 2000, regarding certain limitations on voting and the acquisition of additional shares of common stock, incorporated herein by reference to The Aristotle Corporation's Report on Form 8-K dated May 2, 2000.*

10.1 - The Aristotle Corporation 2002 Employee, Director and Consultant Stock Plan.

10.2 - Form of Non-Qualified Stock Option Agreement (for employees, directors and consultants).

10.3 - Form of Incentive Stock Option Agreement (for employees).

10.4 - Settlement and Release Agreement dated as of May 29, 1996, among The Aristotle Corporation, the Federal Deposit Insurance Corporation and certain other interested parties, incorporated herein by reference to Exhibit 10.22 of The Aristotle Corporation Annual Report on Form 10-K for the fiscal year ended June 30, 1996.*

10.5 - Stipulation and Agreement of Settlement dated as of May 28, 1996, regarding In Re First Constitution Stockholders Litigation, incorporated herein by reference to Exhibit 10.23 of The Aristotle Corporation Annual Report on Form 10-K for the fiscal year ended June 30, 1996.*

10.6 - Stock Purchase Agreement between The Aristotle Corporation and Kevin Sweeney dated as of April 30, 1999, incorporated herein by reference to Exhibit 2.1 of The Aristotle Corporation Current Report on form 8-K dated May 4, 1999, as amended.*

10.7 - The Aristotle Corporation 1997 Employee and Director Stock Plan, incorporated herein by reference to The Aristotle Corporation Registration Statement on Form S-8 dated December 10, 1997.*

10.8(a) - The Employment Agreement dated as of February 1, 2001, by and between The Aristotle Corporation and Paul McDonald, incorporated herein by reference to Exhibit 10.8 of the Registrant's Quarterly Report on Form 10-Q for the fiscal quarter ended March 31, 2001.*

10.8(b) - Amendment, dated June 17, 2002, to the Employment Agreement dated as of February 1, 2001 by and between The Aristotle Corporation and Paul McDonald.

10.9(a) - The Employment Agreement dated as of February 1, 2001, by and between The Aristotle Corporation and John Crawford, incorporated herein by reference to Exhibit 10.9 of The Aristotle Corporation's Annual Report on Form 10-K for the fiscal year ended June 30, 2001.*

10.9(b) - Amendment, dated June 17, 2002, to the Employment Agreement dated as of February 1, 2001 by and between The Aristotle Corporation and John J.

Crawford.

10.10 - Exchange Agreement, dated as of November 27, 2001, between The Aristotle Corporation and Geneve Corporation, incorporated herein by reference to Exhibit 10 of The Aristotle Corporation Current Report on Form 8-K dated November 30, 2001.*

10.11 - Letter Agreement, dated May 24, 2002, between The Aristotle Corporation and Paul McDonald regarding the exercisability of certain stock options.

10.12 - Letter Agreement, dated May 24, 2002, between The Aristotle Corporation and John J. Crawford regarding the exercisability of certain stock options.

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10.13 - Full Recourse Promissory Note, dated June 17, 2002, in the principal amount of $32,837.50, made by Paul McDonald in favor of The Aristotle Corporation.

10.14 - Form of Letter Agreement, dated May 24, 2002, between The Aristotle Corporation and non-employee directors regarding the exercisability of certain stock options.

10.15(a) - Amended and Restated Credit Agreement (5 Year) dated as of May 29, 2001, among Nasco International, Inc., Various Financial Institutions now or hereafter parties thereto, Bank One, Wisconsin, and Bank of America, N.A. incorporated by reference to The Aristotle Corporation's Statement on Form S-4 (File No. 333-86026).*

10.15(b) - First Amendment to Amended and Restated Credit Agreement (Five Year) and Consent, dated as of June 17, 2002, among Nasco International, Inc., Various Financial Institutions now or hereafter parties thereto, Bank One, Wisconsin and Bank of America, N.A.

10.15(c) - Assumption Agreement, dated June 17, 2002, executed by The Aristotle Corporation pursuant to Section 3.1 of the First Amendment to Amended and Restated Credit Agreement (Five Year) and Consent (See Exhibit 10.14(b)).

10.16(a) - Amended and Restated Credit Agreement (364 Days) dated as of May 29, 2001, among Nasco International, Inc., Various Financial Institutions now or hereafter parties thereto, Bank One, Wisconsin, and Bank of America, N.A. incorporated by reference to The Aristotle Corporation's Registration Statement on Form S-4 (File No. 333-86026).*

10.16(b)- Second Amendment to Amended and Restated Credit Agreement (364 Days) and Consent, dated as of June 17, 2002, among Nasco International, Inc., Various Financial Institutions now or hereafter parties thereto, Bank One, Wisconsin and Bank of America, N.A.

10.16(c)- Assumption Agreement, dated June 17, 2002, executed by The Aristotle Corporation pursuant to Section 3.1 of the Second Amendment to Amended and Restated Credit Agreement (364 Days) and Consent (See Exhibit 10.15(b)).

10.17 -Second Amended and Restated Mortgage (and Security Agreement and Assignment of Leases and Rents), dated as of August 21, 2001, by and between Nasco International, Inc., as Mortgagor, in favor of Bank of America, N.A., as agent incorporated by reference to The Aristotle Corporation's Registration Statement on Form S-4 (File No. 333-86026).*

10.18 - Second Amended and Restated Deed of Trust, Security Agreement, Assignment of Rents and Leases, and Fixture Filing, dated as of August 21, 2001, by Nasco International, Inc., as Mortgagor, in favor of Commonwealth Land Title Insurance Company, as Trustee for the benefit of Bank of America, N.A. incorporated by reference to The Aristotle Corporation's Registration Statement on Form S-4 (File No. 333-86026).*

10.19 - Deed of Trust, Security Agreement, Assignment of Rents and Leases, and Fixture Filing, dated as of August 21, 2001, by American Educational Products, Inc., as Mortgagor, in favor of The Public Trustee for the County of Larimer, State of Colorado, as Trustee for the benefit of Bank of America, N.A. incorporated by reference to The Aristotle Corporation's Registration Statement on Form S-4 (File No. 333-86026).*

10.20 - Form of Stockholders Agreement by and among The Aristotle Corporation, Geneve Corporation and Nasco Holdings, Inc., incorporated herein by reference to Exhibit 99.3 of The Aristotle Corporation Current Report on Form 8-K dated November 27, 2001.

10.21 - Assumption of Mortgage and Modification Agreement, dated as of July 12, 2002, by and between The Aristotle Corporation and Bank of America, N.A.

10.22 - Assumption of Deed of Trust and Modification Agreement, dated as of July 12, 2002, by and between The Aristotle Corporation and Bank of America, N.A.

10.23- Assumption of Deed of Trust and Modification Agreement, dated as of July 12, 2002, by and between The Aristotle Corporation and Bank of America, N.A.

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10.24 - Amended and Restated Subsidiary Pledge Agreement, dated as of June 27, 2002, by and between American Educational Products LLC and Bank of America, N.A.

10.25 - Amended and Restated Subsidiary Security Agreement, dated as of June 27, 2002, by and between American Educational Products LLC, the other subsidiaries party thereto and Bank of America, N.A.+

10.26 - Amended and Restated Pledge Agreement, dated as of June 27, 2002, by and between The Aristotle Corporation and Bank of America, N.A.+

10.27 - Amended and Restated Security Agreement, dated as of June 27, 2002, by and between The Aristotle Corporation and Bank of America, N.A.+

99.1 - The Aristotle Corporation's Proxy Statement-Prospectus dated May 15, 2002, incorporated by reference to The Aristotle Corporation's Registration Statement on Form S-4 (File No. 333-86026).*

99.2--Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

* These items are hereby incorporated by reference from the exhibits of the filing or report indicated (except where noted, Commission File No. 0-14669) and are hereby incorporated by reference.

* In accordance with Item 601(b)(2) of Regulation S-K, the schedules have been omitted and a list briefly describing the schedules is at the end of this agreement. Aristotle will furnish supplementally a copy of any omitted schedule to the Comission upon request.

d 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, but not yet vested as of April 1, 2006, 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).

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.

SIGNIFICANT RECENT ACCOUNTING PRONOUNCEMENTS

There were no recent accounting pronouncements issued by the FASB (including its Emerging Issues Task Force), the American Institute of Certified Public Accountants, or the Securities and Exchange Commission during the six months ended September 30, 2013 or that were issued in prior periods but do not become effective until future periods that in the opinion of management had, or are expected to have a material impact on our present or future consolidated financial statements.

NOTE 4. NOTES PAYABLE

Notes payable consist of the following:

	September 30, 2013		March 31, 2013	
	Principal Balance	Accrued Interest	Principal Balance	Accrued Interest
12% Notes payable, past due	$185,000	$339,937	$185,000	$333,000
10% Note payable, past due	5,000	6,125	5,000	6,000
Tonaquint Note	–	–	131,381	543
Directors’ Notes	400,000	9,032	–	–
Total	$590,000	$355,094	$321,381	$339,543

During the six month periods ended September 30, 2013 and 2012, we recorded interest expense of $26,208 and $32,447, respectively, 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. We incurred a loss upon this conversion of $68,703 since the closing price of our common stock was $0.35 at the date of conversion. At September 30, 2013, the 12% Notes were past due, in default, and bearing interest at the default rate of 15%.

10% NOTES

At September 30, 2013, 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.

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During the six months ended September 30, 2013, 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 over the six months ended September 30, 2013.

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

Activity in Tonaquint Note	
Initial principal balance	$360,186
Lender’s legal fees	12,500
Conversions during the fiscal year ended March 31, 2013	(241,307)
Conversions during the six months ended September 30, 2013	(131,379)
Balance as of September 30, 2013	$–

Directors’ Notes

In July 2013, we borrowed $400,000 from two of our directors under 90 day notes bearing 10% interest (the “Notes”). If we do not pay back those loans by October 9, 2013, then the notes will bear interest at a penalty rate of 12% and the noteholders will have the right at their discretion (i) to 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. 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 have reserved 6,931,818 shares of common stock to support the conversion in full of the Notes and accrued interest as well as the exercise in full of the warrants (should such conversion and/or issuance occur). We are discussing an extension on the Director’s Notes.

NOTE 5. CONVERTIBLE NOTES PAYABLE

Convertible notes payable consist of the following at September 30, 2013:

	Principal	Unamortized Discount	Net Amount	Accrued Interest

Amended and Restated Series A 12% Convertible Notes, past due	$885,000	$ –	$885,000	$486,750
December 2006 10% Convertible Notes, past due	17,000	–	17,000	17,163
2008 10% Convertible Notes, past due	25,000	–	25,000	17,292
October & November 2009 10% Convertible Notes	50,000	–	50,000	23,444
April 2010 10% Convertible Note	75,000	(570)	74,430	27,688
September 2010 10% Convertible Notes, past due	283,100	–	283,100	34,536
April 2011 10% Convertible Notes, past due	400,400	–	400,400	80,130
July and August 2011 10% Convertible Notes, $257,656 past due	377,683	–	377,683	73,416
September 2011 Convertible Notes, past due	9,760	–	9,760	–
Law Firm Note Number 1	75,000	–	75,000	5,729
Law Firm Note Number 2	47,000	–	47,000	757
Total – Convertible Notes	$2,244,943	$ (570)	$2,244,373	$766,905

All of the convertible notes payable in the above table are presently past due or will be due within one year of the September 30, 2013 balance sheet date. As a result, we expect to amortize all of the remaining discounts during the fiscal year ending March 31, 2014.

During the six months ended September 30, 2013, we recorded interest expense of $178,788 related to the contractual interest rates of our convertible notes and interest expense of $3,714 related to the amortization of debt discounts on the convertible notes for a total of $91,293.

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	$2,371,915	$ (4,284)	$2,367,631	$698,544

AMENDED AND RESTATED SERIES A 12% CONVERTIBLE NOTES

In June 2010, we entered into Amended and Restated 12% Series A Convertible Promissory Notes (the "Amended and Restated Notes") with the holders of certain promissory notes previously issued by the Company (“Amended Series A 10% Convertible Notes” or the "Prior Notes"), and all amendments to the Prior Notes.

The Amended and Restated Notes, in the principal amount of $900,000 matured on December 31, 2010. In connection with the restructuring 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 ("Units") at a fixed rate of $0.20 per Unit, each Unit consisting 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 as prescribed in the Amended and Restated Note Agreement. The noteholders have antidilution price protection on the Amended and Restated Notes.

In addition to the extension of the expiration date of the Amended and Restated Notes to December 31, 2010, we agreed to increase 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, 2010, the Amended and Restated Notes matured and as of March 31, 2013 remain in default. We are accruing interest at the revised default rate of 20% following the expiration date of December 31, 2010.

During the fiscal year ended March 31, 2013, the holders of $15,000 of the Amended and Restated Notes converted their principal and related accrued interest into common stock per the conversion formula.

We have begun discussions with the noteholders regarding an extension to the notes 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%.

DECEMBER 2006 10% CONVERTIBLE NOTES

At September 30, 2013, one note representing $17,000 of the December 2006 10% Notes remained outstanding and in default. This note is convertible into our common stock at $0.17 per share. We are recording interest at the default rate of 15%.

2008 10% CONVERTIBLE NOTES

One 2008 10% Convertible Note in the amount of $25,000 which matured in January 2010 remained outstanding at September 30, 2013. This 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 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 $25,000 note 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). 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 Note 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)
Conversions during the fiscal year ended March 31, 2012	(130,250)
Conversions during the fiscal year ended March 31, 2013	(25,000)
Balance as of September 30, 2013	$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 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 September 30, 2013, 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. We recorded a charge of $77,265 relating to this modification in the quarter ended March 31, 2012.

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 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. There are no registration requirements with respect to the shares of common stock underlying the notes or the warrants.

The following table shows the conversions into principal of the September 2010 10% Convertible Notes Note 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)
Balance as of September 30, 2013	$308,100

$25,000 of the September 2010 10% Convertible Notes converted to common stock during the six months ended September 30, 2013. We are recording interest at the default rate of 15%.

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 ten percent (10%) 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 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.

As of September 30, 2013, there have not been any conversions of the April 2011 10% Convertible Notes. We are recording interest at the default rate of 15%.

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.

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 have not been any conversions of the July & August 2011 10% Convertible Notes.

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.

At September 30, 2013, the outstanding principal balance was $377,683, of which $257,655 was in default. Following the expiration of the maturity dates on the $257,655 of notes that are now in default, we began to accrue 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 (the "Purchasers") 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 mature 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. There are no registration requirements with respect to the shares of common stock underlying the notes or the warrants.

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.

The following table shows the conversions into principal of the September 2011 Convertible Notes Note 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 six months ended September 30, 2013	(169,000)
Balance as of September 30, 2013	$9,760

At September 30, 2013, the outstanding principal balance was in default and there was no accrued interest as these notes do not bear interest.

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. 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. This ability of the holder to convert became exercisable upon the amendment of the Articles of Incorporation increasing the authorized shares of our common stock to a number greater than 250,000,000. As that increase in the authorized number of shares of our common stock was approved by our stockholders at a Special Stockholders Meeting on June 4, 2012, this note was reclassified to a convertible note as of June 30, 2012. 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. As of September 30, 2013, there have not been any conversions of the Law Firm Note Number 1.

At September 30, 2013, the outstanding principal balance was $75,000.

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 has a maturity date of October 1, 2014 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 $0.07 per share. As of September 30, 2013, there have not been any conversions of the Law Firm Note Number 2.

At September 30, 2013, the outstanding principal balance was $47,000.

NOTE 6. EQUITY TRANSACTIONS

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.

In June 2013, we completed a unit subscription agreement with three accredited investors (the “Purchasers”) pursuant to which the Purchasers purchased $128,000 of units (the "Units" and each a "Unit"), with each Unit consisting of (i) one share of Common Stock at a price per share of $0.081 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) $0.081 (the "Warrant

Shares") at an exercise price of $0.121 per Warrant Share. This resulted in the issuance of 1,580,248 shares of Common Stock and 790,124 Warrant Shares.

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 3,448,337 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 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).

In August 2013, we completed a unit subscription agreement with four accredited investors (the “Purchasers”) pursuant to which the Purchasers purchased $100,000 of units (the "Units" and each a "Unit"), with each Unit consisting of (i) one share of Common Stock at a price per share of $0.111 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) $0.111 (the "Warrant Shares") at an exercise price of $0.167 per Warrant Share. This resulted in the issuance of 900,901 shares of Common Stock and 450,451 Warrant Shares.

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, 18 warrant holders exercised 6,581,259 warrants to receive 3,407,468 restricted shares of common stock in cashless transactions.

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.

NOTE 7. ACCRUED LIQUIDATED DAMAGES

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 we will become obligated for future payments and the amount, or range of amounts, of such future payments can be reasonably estimated.

We have entered into registration payment arrangements in connection with certain financing arrangements, pursuant to which we raised an approximate aggregate amount of $2,020,000, that require us to register the shares of common stock underlying the convertible debt and warrants issued in these financing transactions. Under these agreements we are liable for liquidated damages to the investors if we fail to file and/or maintain effective registration statements covering the specified underlying shares of common stock as noted below:

- With respect to a $1,000,000 financing agreement – damages accrue at a rate of 1% - 1.5% per month until such time as the underlying shares of common stock would have been eligible for sale under Rule 144.
- With respect to financing agreements totaling $715,000 – damages accrue at a rate of 2% per month, subject to an aggregate maximum liquidated damages amount of $150,000.
- With respect to equity investments totaling $305,000 – damages accrue at a rate of 2% per month until the expiration dates of warrants issued in connection with this financing, which range from December 31,2010 through February 8, 2011 and are payable in common stock.

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Since we have either failed to file, or failed to maintain the registration obligations under these agreements, as of September 30, 2013 and March 31, 2013, we have accrued estimated aggregate liquidated damages of $437,800 in connection with the liquidated damage provisions of these agreements, which we believe represents our maximum exposure under these provisions. Accordingly, we do not expect to accrue any further liquidated damages in connection with these agreements. The actual amount of liquidated damages paid, if any, may differ from our estimates as it is our intention to negotiate with the investors the settlement of liquidated damages due and, as such, the ultimate amounts we may actually pay may be less than the amount currently accrued.

NOTE 8. OTHER CURRENT LIABILITIES

At September 30, 2013 and March 31, 2013, our other current liabilities were comprised of the following items:

	September 30, 2013	March 31, 2013
Accrued interest	$1,126,909	$1,032,110
Accrued legal fees	179,465	179,465
Other	79,460	155,610
Total other current liabilities	$1,385,834	$1,367,185

As of the date of this report, various promissory and convertible notes payable in the aggregate principal amount of $2,067,916 (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, 2013, we had accrued interest in the amount of $1,052,865 associated with these defaulted notes in accrued liabilities payable (see Notes 4 and 5).

NOTE 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.

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 September 30, 2013 reporting date are classified based on the valuation technique level noted in the table below (there were no transfers in or out of level 3 for all periods presented):

Description	September 30, 2013	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Derivative Liabilities	$5,864,615	$ –	$ –	$ 5,864,615
Total Assets	$5,864,615	$ –	$ –	$ 5,864,615

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:

	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, 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

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, 2012:

	April 1, 2012	Recorded New Derivative Liabilities	Change in estimated fair value recognized in results of operations	Reclassification of Derivative Liability to Paid in capital	September 30, 2012
Derivative liabilities	$3,588,615	$ –	$(361,462)	$(32,759)	$3,194,394

The fair value of derivative liabilities that we recorded in the six months ended September 30, 2012 was related to our April 2011 convertible note, July & August 2011 10% convertible notes and the September 2011 convertible note offerings (see Note 5) and was based upon an independent valuation report.

NOTE 10. STOCK COMPENSATION

The following table summarizes 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 September 30, 2013 and 2012:

	Three Months Ended September 30, 2013	Three Months Ended September 30, 2012	Six Months Ended September 30, 2013	Six Months Ended September 30, 2012
Total share-based compensation expense	$ 74,813	$ 226,196	$ 190,601	$ 395,495
Total share-based compensation expense included in net loss	$ 74,813	$ 226,196	$ 190,601	$ 395,495
Basic and diluted loss per common share	$ (0.00)	$ (0.00)	$ (0.00)	$ (0.00)

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 September 30, 2013 and 2012.

	Three Months Ended September 30, 2013	Three Months Ended September 30, 2012	Six Months Ended September 30, 2013	Six Months Ended September 30, 2012
Vesting of stock options	73,856	128,572	124,243	181,047
Incremental fair value of option modifications	957	957	1,914	21,114
Vesting expense associated with CEO restricted stock grant	–	96,667	64,444	193,334
Total share-based compensation expense	$ 74,813	$ 226,196	$ 190,601	$ 395,495
Total share-based compensation expense included in net loss	$ 74,813	$ 226,196	$ 190,601	$ 395,495
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, 2013 and 2012, which totaled $190,601 and $395,495, respectively, is included in payroll and related expense in the accompanying condensed consolidated statements of operations. Stock-based compensation expense recorded during the three and six months ended September 30, 2013 and 2012 had no impact on basic and diluted loss per common share.

In the six months ended September 30, 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.

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:

Risk free interest rate	0.38% - 2.50%
Average expected life	3 years - 10 years
Expected volatility	94.6% - 102.7%
Expected dividends	None

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 six months ended September 30, 2013 was insignificant.

The expected volatility is based on the historic volatility. The expected life of options granted is 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, 2013 are as follows:

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term in Years
Vested	20,949,956	$ 0.28	3.77
Expected to vest	3,770,842	$ 0.11	9.69
Total	24,720,798	$ 0.26	4.68

A summary of stock option activity during the six months ended September 30, 2013 is presented below:

	Number of Options	Range of Exercise Price	Weighted Average Exercise Price
Stock options outstanding at March 31, 2013	21,095,798	$0.076 - $0.41	$ 0.28
Exercised	–	–	
Issued	3,625,000	$0.10 - 0.11	$ 0.10
Cancelled/Expired	–	–	
Stock options outstanding at September 30, 2013	24,720,798	$0.076 - $0.41	$ 0.26
Stock options exercisable at September 30, 2013	20,949,956	$0.076 - $0.41	$ 0.28

At September 30, 2013, there was approximately $337,279 of unrecognized compensation cost related to share-based payments which is expected to be recognized over a weighted average period of 1.13 years.

On September 30, 2013, 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

NOTE 11. WARRANTS

A summary of warrant activity during the six months ended September 30, 2013 is presented below:

	Number of Warrants	Range of Exercise Price	Weighted Average Exercise Price
Warrants outstanding at March 31, 2013	75,647,294	$0.076 - $0.25	$0.11
Exercised	(3,407,468)	$0.11	$0.11
Issued	3,513,302	$0.121-$0.167	$0.13
Cancelled/Expired	(3,173,791)	$0.11	$0.11
Warrants outstanding at September 30, 2013	72,579,337	$0.076 - $0.25	$0.12
Warrants exercisable at September 30, 2013	72,579,337	$0.076 - $0.25	$0.12

The following outlines the significant weighted average assumptions used to estimate the fair value information, which is based on historical data, with respect to warrants utilizing the Binomial Lattice option pricing models at, and during the six months ended September 30, 2013:

Risk free interest rate	1.53% - 2.04%
Average expected life	7 years
Expected volatility	91.2 – 96.0%
Expected dividends	None

NOTE 12. DARPA CONTRACT AND RELATED REVENUE RECOGNITION

As discussed in Note 3, 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 is a fixed-price contract with potential total payments to us of $6,794,389 over the course of five years, including payments of up to $1,975,047 in the first year. 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.

The details of the four milestones achieved during the six month period ended September 30, 2013 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 > 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.

NOTE 13. COMMITMENTS AND CONTINGENCIES

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 July 5, 2012, Gemini Master Fund, Ltd., a Cayman Islands company ("Gemini"), filed a complaint against the Company 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 is seeking relief both in the form of money damages and delivery of shares of the Company's common stock. The Complaint alleges, among other things, that the Company is in default of a certain promissory note originally issued to Gemini on February 12, 2010 by failing to pay the note in full and by failing to honor certain requests by Gemini to convert principal and interest under the note into shares of the Company's common stock. The Complaint also alleges that the Company failed to issue shares upon the presentation of an exercise notice under a warrant originally issued to Gemini on November 22, 2010. The lawsuit also alleges that the Company should have issued shares pursuant to the exercise of a warrant issued in 2009. The Company believes that it has defenses to the claims asserted and it continues to vigorously defend the lawsuit, which is in the late discovery stage. No trial date has yet been set. There can be no assurances, however, that the litigation will be decided in the Company's favor as to all, or any part, of Gemini's Complaint. An adverse decision in the litigation could have an adverse effect on the Company's operations and could be dilutive to the Company's shareholders.

LEASES

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 $7,299 per month on a lease that expires in September 2014 based on a one year extension signed in August 2013.

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.

In October 2013, our Exosome Sciences, Inc. (ESI) subsidiary entered into a one year lease for approximately 2,055 square feet of laboratory space at 11 Deer Park Drive, Suite 103, Monmouth Junction, New Jersey 08852 at the rate of $3,425 per month.

NOTE 14. SUBSEQUENT EVENTS

Management has evaluated events subsequent to September 30, 2013 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.

In October 2013 and through November 13, 2013, we collected $233,271 under our government contracts.

On October 30, 2013, we entered into a unit purchase agreement (the “Unit Purchase Agreement”) and subscription agreements (the “Subscription Agreements”) with three accredited investors (collectively, the “Purchasers”), pursuant to which the Purchasers purchased an aggregate of 18.4 units (collectively, the “Units”) from us, with each Unit consisting of (a) one hundred thousand (100,000) shares of our common stock, par value $.001 per share (the “Common Stock”), at a purchase price of $0.125 per share and (b) a warrant to purchase fifty thousand (50,000) shares of Common Stock (collectively, the “Warrants”). The Purchasers acquired an aggregate of 1,840,000 shares of Common Stock and Warrants to acquire up to an aggregate of 920,000 shares of Common Stock for an aggregate purchase price of $230,000. Each Warrant is exercisable for a period of five years from the date of issuance at an exercise price of $0.22, subject to adjustment. A Purchaser may exercise a Warrant on a cashless basis. In the event a Purchaser exercises a Warrant on a cashless basis, we will not receive any proceeds. The exercise price of the Warrants is subject to customary adjustments provisions for stock splits, stock dividends, recapitalizations and the like. There are no registration rights associated with the Common Stock or the Warrants.

Each Purchaser has contractually agreed to restrict its ability to exercise its Warrant such that the number of shares of the Common Stock held by the Purchaser and its affiliates after such exercise does not exceed 4.99% of our then issued and outstanding shares of Common Stock.

A FINRA registered broker-dealer was engaged as placement agent in connection with the private placement. We paid the placement agent a cash fee in the amount of $52,600 (representing a $25,000 activation fee, a 10% sales commission, and a 2% non-allocable expense allowance) and will issue the placement agent or its designees warrants to purchase an aggregate of 276,000 shares of Common Stock at $0.22 per share. The warrants issued to the placement agent may be exercised on a cashless basis. In the event the placement agent exercises the warrants on a cashless basis, we will not receive any proceeds.

On October 8, 2013, October 17, 2013 and October 23, 2013, our subsidiary, Exosome Sciences, Inc., issued a total of 3 promissory notes (collectively, the “Notes”) in the aggregate principal amount of $250,000 to Dr. Chetan Shah, a director of the Company, in exchange for Dr. Shah’s loan of funds in the same aggregate amount to ESI. Each Note bears interest at the rate of 10% per annum and will be due and payable in full, including all accrued interest thereon, one year from the date of issuance. The Notes are unsecured and do not provide for conversion of the debt into any other security. The Notes have not been guaranteed by the Company.

In October 2013, our Exosome Sciences, Inc. (ESI) subsidiary entered into a one year lease for approximately 2,055 square feet of laboratory space at 11 Deer Park Drive, Suite 103, Monmouth Junction, New Jersey 08852.

In October 2013, a warrant holder exercised 2,805,000 warrants to receive 1,577,736 shares in a cashless transaction.

In October 2013, we issued 549,450 shares of restricted common stock to the holder of a note issued by the Company in exchange for the partial conversion of accrued interest in an aggregate amount of $30,000 at an average conversion price of $0.05 per share.

On November 12, 2013, we entered into a unit purchase agreement (the “Unit Purchase Agreement”) and subscription agreements (the “Subscription Agreements”) with eight accredited investors (collectively, the “Purchasers”), pursuant to which the Purchasers purchased an aggregate of 32.96 units (collectively, the “Units”) from us, with each Unit consisting of (a) one hundred thousand (100,000) shares of our common stock, par value $.001 per share (the “Common Stock”), at a purchase price of $0.125 per share and (b) a warrant to purchase fifty thousand (50,000) shares of Common Stock (collectively, the “Warrants”). The Purchasers acquired an aggregate of 3,296,000 shares of Common Stock and Warrants to acquire up to an aggregate of 1,648,000 shares of Common Stock for an aggregate purchase price of $412,000. Each Warrant is exercisable for a period of five years from the date of issuance at an exercise price of $0.22, subject to adjustment. A Purchaser may exercise a Warrant on a cashless basis. In the event a Purchaser exercises a Warrant on a cashless basis, we will not receive any proceeds. The exercise price of the Warrants is subject to customary adjustments provisions for stock splits, stock dividends, recapitalizations and the like. There are no registration rights associated with the Common Stock or the Warrants.

Each Purchaser has contractually agreed to restrict its ability to exercise its Warrant such that the number of shares of the Common Stock held by the Purchaser and its affiliates after such exercise does not exceed 4.99% of our then issued and outstanding shares of Common Stock.

A FINRA registered broker-dealer was engaged as placement agent in connection with the private placement. We paid the placement agent a cash fee in the amount of $61,940 (representing a $12,500 advisory fee, a 10% sales commission, and a 2% non-allocable expense allowance) and will issue the placement agent or its designees warrants to purchase an aggregate of 494,400 shares of Common Stock at $0.22 per share. The warrants issued to the placement agent may be exercised on a cashless basis. In the event the placement agent exercises the warrants on a cashless basis, we will not receive any proceeds.

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

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

FORWARD LOOKING STATEMENTS

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

THE COMPANY

Aethlon Medical, Inc. ("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.

In June 2013, the U.S. Food and Drug Administration ("FDA") approved our Investigational Device Exemption ("IDE") application to initiate a ten patient human clinical trial in one location in the United States. Successful outcomes of that human trial as well as at least one follow-on human trial will be required by the FDA in order to commercialize our products in the US. 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 FDA 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(R) treatment technology.

In prior periods, Aethlon was classified as a development stage enterprise under accounting principles generally accepted in the United States of America ("GAAP") as it had not generated revenues from its planned principal operations. In the fiscal year ended March 31, 2012, we began to generate revenues from a government contract and have emerged from the development stage.

WHERE YOU CAN FIND MORE INFORMATION

We are subject to the informational requirements of the Securities Exchange Act and must file reports, proxy statements and other information with the SEC. The reports, information statements and other information we file with the Commission can be inspected and copied at the Commission Public Reference Room, 100 F Street, N.E., Washington, D.C. 20549. You may obtain information on the operation of the Public Reference Room by calling the SEC at (800) SEC-0330. The Commission also maintains a Web site (http://www.sec.gov) that contains reports, proxy and information statements and other information regarding registrants, like us, which file electronically with the Commission. Our headquarters are located at 8910 University Center Lane, Suite 660, San Diego, CA 92122. Our phone number at that address is (858) 459-7800. Our Web site is http://www.aethlonmedical.com.

RESULTS OF OPERATIONS

THREE MONTHS ENDED SEPTEMBER 30, 2013 COMPARED TO THE THREE MONTHS ENDED SEPTEMBER 30, 2012

Revenues

We recorded government contract revenue of $644,887 and $400,114 in the three months ended September 30, 2013 and 2012, respectively. This revenue arose from work performed under our government contract with DARPA and our subcontract with Battelle as follows:

	Three Months Ended 9/30/13	Three Months Ended 9/30/12	Change in Dollars
DARPA Contract	$613,143	$400,114	$213,029
Battelle Subcontract	31,744	–	31,744
Total Government Contract Revenue	$644,887	$400,114	$244,773

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DARPA - On September 30, 2011, we entered into a contract with the United States of America, issued by SPAWAR Systems Center Pacific, pursuant to a contract award from the Defense Advanced Research Projects Agency ("DARPA"). 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 is a fixed-price contract with potential total payments to us of $6,794,389 over the course of five years, including payments of up to $1,975,047 in the first year. 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.

As of September 30, 2013, we have invoiced for fifteen milestone payments under the DARPA contract totaling $3,396,912.

Battelle -- 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 under a time and materials basis and we began generating revenues under the subcontract in the three months ended September 30, 2013. Our expected revenue from the subcontract will be at the discretion of Battelle. The Battelle subcontract is our first cost-reimbursable contract.

Our revenue under this contract will be 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.

Operating Expenses

Consolidated operating expenses for the three months ended September 30, 2013 were $874,683 in comparison with $1,199,908 for the comparable quarter a year ago. This decrease of $325,225, or 27.1%, was due to decreases in payroll and related expenses of $154,621, in professional fees of $123,488 and in general and administrative expenses of $47,116.

The $154,621 decrease in payroll and related expenses was primarily due to a decrease in stock based compensation of $151,383, which in turn was due to the completion of the vesting of our CEO's restricted stock grant and of the vesting of a number of existing stock option grants.

The $123,488 decrease in our professional fees was due to a reduction of DARPA contract related professional fees of $72,015 and a reduction of non-DARPA related professional fees of $51,473. The primary drivers in the decrease in non-DARPA related professional fees were the lack of legal fees related to the Gemini litigation and to work on resolving our DTC suspension as our insurance carrier has covered the litigation costs in the 2013 period and we successfully resolved the DTC suspension in the fiscal year ended March 31, 2013.

The $47,116 decrease in general and administrative expenses was due to a reduction of non-DARPA related general and administrative expenses of $35,395 and to a reduction of DARPA contract related general and administrative expenses of $11,721.

Other Expense (Income)

Other expense (income) consists primarily of the change in the fair value of our derivative liability, other expense and interest expense. Other expense (income) for the three months ended September 30, 2013 were other expense of $3,119,874 in comparison with other expense of $621,530 for the comparable quarter a year ago.

Change in Fair Value of Derivative Liability

Both periods include changes in the fair value of derivative liability. For the three months ended September 30, 2013, the change in the estimated fair value of derivative liability was a charge of $2,992,002 and for the three months ended September 30, 2012, the change in estimated fair value was a charge of $326,138.

Interest Expense

Interest expense was $110,405 for the three months ended September 30, 2013 compared to $224,374 in the corresponding prior period, a decrease of $113,969. The various components of our interest expense are shown in the following table:

	Quarter Ended 9/30/13	Quarter Ended 9/30/12	Change
Interest Expense	$108,723	$126,100	$(17,377)
Amortization of Deferred Financing Costs	–	22,739	(22,739)
Amortization of Note Discounts	1,682	75,535	(73,853)
Total Interest Expense	$110,405	$224,374	$(113,969)

As noted in the above table, the two most significant factors in the $113,969 decrease in interest expense were (a) the $73,853 reduction in the amortization of debt discounts that was largely the result of the completion of the discount amortization on the majority of our convertible notes prior and (b) a $22,739 reduction in the amortization of deferred offering costs that also was largely the result of the completion of the amortization on those costs.

Other

The three months ended September 30, 2013 contained $17,467 in losses on debt conversion compared to a $71,080 loss on debt conversion in the three months ended September 30, 2012.

Net Loss

As a result of the increased expenses noted above, we recorded a consolidated net loss of approximately $3,350,000 and $1,421,000 for the quarters ended September 30, 2013 and 2012, respectively.

Basic and diluted loss per common share were ($0.02) for the three month period ended September 30, 2013 compared to ($0.01) for the period ended September 30, 2012.

SIX MONTHS ENDED SEPTEMBER 30, 2013 COMPARED TO THE SIX MONTHS ENDED SEPTEMBER 30, 2012

Revenues

We recorded government contract revenue of $840,483 and $616,861 in the six months ended September 30, 2013 and 2012, respectively. This revenue arose from work performed under our government contract with DARPA and our subcontract with Battelle as follows:

	Six Months Ended 9/30/13	Six Months Ended 9/30/12	Change in Dollars
DARPA Contract	$808,739	$616,861	$191,878
Battelle Subcontract	31,744	–	31,744
Total Government Contract Revenue	$840,483	$616,861	$223,622

DARPA - On September 30, 2011, we entered into a contract with the United States of America, issued by SPAWAR Systems Center Pacific, pursuant to a contract award from the Defense Advanced Research Projects Agency (“DARPA”). 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 is a fixed-price contract with potential total payments to us of $6,794,389 over the course of five years, including payments of up to $1,975,047 in the first year. 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.

As of September 30, 2013, we have invoiced for fifteen milestone payments under the DARPA contract totaling $3,396,912.

Battelle -- 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 under a time and materials basis and we began generating revenues under the subcontract in the three months ended September 30, 2013. Our expected revenue from the subcontract will be at the discretion of Battelle. The Battelle subcontract is our first cost-reimbursable contract.

Our revenue under this contract will be 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.

Operating Expenses

Consolidated operating expenses for the six months ended September 30, 2013 were $1,854,075 in comparison with $2,408,444 for the comparable period a year ago. This decrease of $554,369, or 23.0%, was due to decreases in professional fees of $276,539, in payroll and related expenses of $250,086 and general and administrative expenses of $27,744.

The $276,539 decrease in our professional fees was primarily due to a reduction of non-DARPA related professional fees of $242,752 and a reduction in DARPA contract related professional fees of $33,787. The primary drivers in the decrease in non-DARPA related professional fees were the lack of legal fees related to the Gemini litigation and to work on resolving our DTC suspension as our insurance carrier has covered the litigation costs in the 2013 period and we successfully resolved the DTC suspension in the fiscal year ended March 31, 2013.

The $250,086 decrease in payroll and related expenses was primarily due to a decrease in stock based compensation of $204,894, which in turn was due to the completion of the vesting of our CEO’s restricted stock grant and of the vesting of a number of existing stock option grants. The $45,192 reduction in cash based compensation was primarily driven by a $32,000 reduction in bonus payments to our management team.

The $27,744 decrease in general and administrative expenses was driven by a $40,795 reduction of non-DARPA related general and administrative expenses, which was partially offset by a $13,051 increase in DARPA-related general and administrative expenses.

Other Expense (Income)

Other expense (income) consists primarily of the change in the fair value of our derivative liability, other expense and interest expense. Other expense (income) for the six months ended September 30, 2013 were other expense of $2,639,576 in comparison with other expense of $647,552 for the comparable period a year ago.

Change in Fair Value of Derivative Liability

Both periods include changes in the fair value of derivative liability. For the six months ended September 30, 2013, the change in the estimated fair value of derivative liability was a charge of $2,382,877 and for the six months ended September 30, 2012, the change in estimated fair value was a gain of $361,462.

Interest Expense

Interest expense was $216,502 for the six months ended September 30, 2013 compared to $913,062 in the corresponding prior period, a decrease of $696,560. The various components of our interest expense are shown in the following table:

	6 Months Ended 9/30/13	6 Months Ended 9/30/12	Change
Interest Expense	$211,924	$318,719	$(106,795)
Amortization of Deferred Financing Costs	863	120,790	(119,927)
Non-Cash Interest Expense	–	11,846	(11,846)
Amortization of Note Discounts	3,715	461,707	(457,992)
Total Interest Expense	$216,502	$913,062	$(696,560)

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As noted in the above table, the three most significant factors in the $696,560 decrease in interest expense were (a) the $457,992 reduction in the amortization of debt discounts that was largely the result of the completion of the discount amortization on the majority of our convertible notes prior, (b) a $119,927 reduction in the amortization of deferred offering costs that also was largely the result of the completion of the amortization on those costs and (c) the $106,795 reduction in interest expense due to ongoing conversions of our convertible notes into equity.

Other

The six months ended September 30, 2013 contained $40,257 in losses on debt conversion compared to a $96,059 loss on debt conversion in the six months ended September 30, 2012.

Net Loss

As a result of the increased expenses noted above, we recorded a consolidated net loss of approximately $3,653,000 and $2,439,000 for the six month periods ended September 30, 2013 and 2012, respectively.

Basic and diluted loss per common share were ($0.02) for the six month period ended September 30, 2013 compared to ($0.02) for the period ended September 30, 2012.

LIQUIDITY AND CAPITAL RESOURCES

At September 30, 2013, we had a cash balance of $8,754 and a working capital deficit of $11,674,899. This compares to a cash balance of $125,274 and a working capital deficit of $9,276,618 at March 31, 2013. Between October 1, 2013 and November 13, 2013, we raised $492,460 in equity and received a total of $233,271 under our DARPA and Battelle contracts. Our cash at September 30, 2013 plus additional funds raised to date subsequent to September 30, 2013 are not sufficient to meet our funding requirements during the next twelve months. Significant additional financing must be obtained in order to provide a sufficient source of operating capital and to allow us to continue to operate as a going concern.

In August 2013, we signed an agreement with a broker-dealer to raise operating capital, of which the $642,000 in gross proceeds ($472,460 in net proceeds) raised through the date of this filing is the initial portion, to cover near term operating requirements and the expected costs of our US safety trial. The agreement also calls for the broker-dealer to then raise a larger financing (see note 2) to meet future growth initiatives. Any securities offered will not be registered under the Securities Act and may not be offered or sold in the United States absent registration or an applicable exemption from registration requirements. The engagement agreement is on a best efforts basis and there can be no assurance that the broker-dealer can raise working capital for us on acceptable terms or at all.

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 options for years four and five of our DARPA contract, the effects would be material to us. The loss of revenues from the DARPA contract would have a material impact on our revenues, operating cash flows and liquidity.

DARPA recently awarded a related contract to Battelle Memorial Institute (“Battelle”) to be the systems integrator for the various components being developed under the original contract, including our two components of the project. We agreed to become a subcontractor to Battelle under that systems integrator contract. That subcontract will be under a cost plus basis and we expect to begin generating revenues under the subcontract during the fiscal year ending March 31, 2014. Any revenues we derive under the subcontract will be at the direction of Battelle.

Beyond the immediate future, we currently believe that the following four areas may generate revenue for us:

(1) Developing future products using the Aethlon ADAPTTM system with drug industry collaborators. Revenues in this area could come from product development fees, fees from research, regulatory and manufacturing support or from downstream royalties;

(2) Applying for and winning additional U.S. Government grant or contract income;

(3) Licensing or selling our ELLSA research diagnostic tools that identify and quantify exosomes through our recently launched ESI subsidiary; and

(4) Commercializing the Hemopurifier® in India following a successful result in our Hepatitis-C-oriented clinical trial currently being conducted at the Medanta Medicity Institute (Medicity) in that country. Medicity's Institutional Review Board has agreed to allow compassionate usage of the Hemopurifier® for individuals who previously failed or subsequently relapsed standard-of-care drug regimens. In addition to offering Hemopurifier® therapy to the citizens of India, HCV-infected individuals from the United States, European Union and other regions of the world may pursue treatment through the expanded access program at Medicity.

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 30, 2013	September 30, 2012
Cash (used in) provided by:		
Operating activities	$(745)	$ (915)
Investing activities	–	–
Financing activities	628	1,043
Net (decrease) increase in cash	$(117)	$ 128

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 $745,000 in the six months ended September 30, 2013 compared to net cash used in operating activities of approximately $915,000 in the six months ended September 30, 2012, a decrease of $171,000. The $171,000 decrease was primarily due to an increase in our government contract revenue of approximately $224,000 and a reduction in our operating expenses of approximately $554,000 which were partially offset by a reduction in our non-cash stock based compensation expense of approximately $205,000 and a reduction in our accounts receivable of approximately $412,000.

NET CASH FROM INVESTING ACTIVITIES. During the six months ended September 30, 2013, we did not have any investing activities. During the six months ended September 30, 2012, we did not have any investing activities.

NET CASH FROM FINANCING ACTIVITIES. Net cash generated from financing activities decreased from approximately $1,043,000 in the six months ended September 30, 2012 to approximately $628,000 in the six months ended September 30, 2013. Included in net cash provided by financing activities in the 2013 period was $400,000 in notes payable from two directors and $228,000 in proceeds from the issuance of common stock. In the 2012 period, we received $1,073,000 in proceeds 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.

A decrease in working capital during the six months ended September 30, 2013 in the amount of approximately $2,398,000 changed our negative working capital position to approximately ($11,675,000) at September 30, 2013 from a negative working capital of approximately ($9,277,000) at March 31, 2013. The most significant factor in the increase in working capital noted above was an increase of approximately $2,276,000 in the fair value of derivative liabilities. That increase was largely driven by the increase in our share price from March 31, 2013 to September 30, 2013.

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

The preparation of condensed consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires the Company 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 policies relate to revenue recognition, measurement of stock purchase warrants issued with notes payable, beneficial conversion feature of convertible notes payable, impairment of intangible assets and long lived assets, stock compensation, and the classification of warrant obligations, and evaluation of contingencies. We believe estimates and assumptions related to these critical accounting policies are appropriate under the circumstances; however, should future events or occurrences result in unanticipated consequences, there could be a material impact on our future financial condition or results of operations.

There have been no changes to our critical accounting policies as disclosed in our Form 10-K for the year ended March 31, 2013.

OFF-BALANCE SHEET ARRANGEMENTS

We have no obligations required to be disclosed herein as off-balance sheet arrangements.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

As a Smaller Reporting Company as defined by rule 12b-2 of the Exchange Act and in Item 10(f)(1) of Regulation S-K, we are electing scaled disclosure reporting obligations and therefore are not required to provide the information requested by this item.

ITEM 4. CONTROLS AND PROCEDURES.

DISCLOSURE CONTROLS AND PROCEDURES

Under the supervision and with the participation of our management, including our Chief Executive Officer ("CEO") and our Chief Financial Officer ("CFO"), we evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Exchange Act) as of a date as of the end of the period covered by this Quarterly Report.

Based on such evaluation, our CEO and CFO concluded that, as of the end of such period, our disclosure controls and procedures are not effective in recording, processing, summarizing and reporting, on a timely basis, information required to be disclosed by us in the reports that we file or submit under the Exchange Act and are not effective in ensuring that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our CEO and CFO, as appropriate to allow timely decisions regarding required disclosure.

CHANGES IN INTERNAL CONTROL OVER FINANCIAL REPORTING

There have been no changes in our internal control over financial reporting during the last fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS.

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 set forth here, we are not presently a party to any pending or threatened legal proceedings.

On July 5, 2012, Gemini Master Fund, Ltd., a Cayman Islands company ("Gemini"), filed a complaint against the Company 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 is seeking relief both in the form of money damages and delivery of shares of the Company's common stock. The Complaint alleges, among other things, that the Company is in default of a certain promissory note originally issued to Gemini on February 12, 2010 by failing to pay the note in full and by failing to honor certain requests by Gemini to convert principal and interest under the note into shares of the Company's common stock. The Complaint also alleges that the Company failed to issue shares upon the presentation of an exercise notice under a warrant originally issued to Gemini on November 22, 2010. The lawsuit also alleges that the Company should have issued shares pursuant to the exercise of a warrant issued in 2009. The Company believes that it has defenses to the claims asserted and it continues to vigorously defend the lawsuit, which is in the late discovery stage. No trial date has yet been set. There can be no assurances, however, that the litigation will be decided in the Company's favor as to all, or any part, of Gemini's Complaint. An adverse decision in the litigation could have an adverse effect on the Company's operations and could be dilutive to the Company's shareholders.

ITEM 1A. RISK FACTORS.

As a Smaller Reporting Company as defined by rule 12b-2 of the Exchange Act and in Item 10(f)(1) of Regulation S-K, we are electing scaled disclosure reporting obligations and therefore are not required to provide the information requested by this item.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.

During the six months ended September 30, 2013, we issued the following securities which were not registered under the Securities Act of 1933, as amended, and have not been included previously in a Current Report on Form 8-K. We did not employ any form of general solicitation or advertising in connection with the offer and sale of the securities described below. In addition, we believe the purchasers of the securities are "accredited investors" for the purpose of Rule 501 of the Securities Act. For these reasons, among others, the offer and sale of the following securities were made in reliance on the exemption from registration provided by Section 4(2) of the Securities Act or Regulation D promulgated by the SEC under the Securities Act:

In June 2013, we completed a unit subscription agreement with three accredited investors (the “Purchasers”) pursuant to which the Purchasers purchased $128,000 of units (the "Units" and each a "Unit"), with each Unit consisting of (i) one share of Common Stock at a price per share of $0.081 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) $0.081 (the "Warrant Shares") at an exercise price of $0.121 per Warrant Share. This resulted in the issuance of 1,580,248 shares of Common Stock and 790,124 Warrant Shares.

During the three months ended June 30 2013, we issued 3,448,337 shares of restricted common stock to the holders of three notes issued by the Company in exchange for the partial or full conversion of principal and interest in an aggregate amount of $246,500 at an average conversion price of $0.07 per share.

In August 2013, we completed a unit subscription agreement with four accredited investors (the “Purchasers”) pursuant to which the Purchasers purchased $100,000 of units (the "Units" and each a "Unit"), with each Unit consisting of (i) one share of Common Stock at a price per share of $0.111 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) $0.111 (the "Warrant Shares") at an exercise price of $0.167 per Warrant Share. This resulted in the issuance of 900,901 shares of Common Stock and 450,451 Warrant Shares.

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, 18 warrant holders exercised 6,581,259 warrants to receive 3,407,468 shares in cashless transactions.

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.

In July 2013, we borrowed $400,000 from two of our directors under 90 day notes bearing 10% interest (the “Notes”). If we do not pay back those loans by October 9, 2013, then the notes will bear interest at a penalty rate of 12% and the noteholders will have the right at their discretion (i) to 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. 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 have reserved 6,931,818 shares of common stock to support the conversion in full of the Notes and accrued interest as well as the exercise in full of the warrants (should such conversion and/or issuance occur). We are discussing an extension on the Director’s Notes.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES.

As of the date of this report, various promissory and convertible notes payable in the aggregate principal amount of $2,067,916 have reached maturity and are past due. We are continually reviewing other financing arrangements to retire all past due notes. At September 30, 2013, we had accrued interest in the amount of $1,052,865 associated with these notes and accrued liabilities payable.

ITEM 4. MINE SAFETY DISCLOSURES.

We have no disclosure applicable to this item.

ITEM 5. OTHER INFORMATION.

In October 2013, Dr. Chetan Shah was named the chair of our Board’s compensation committee.

ITEM 6. EXHIBITS.

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

3.1	Articles of Incorporation of Aethlon Medical, Inc., as amended (1)
3.2	Bylaws of Aethlon Medical, Inc. (2)
4.1	Form of Common Stock Purchase Warrant dated October 30, 2013 (3)
10.1	Form of Unit Purchase Agreement dated October 30, 2013 (3)
10.2	Form of Subscription Agreement dated October 30, 2013 (3)
10.3	Form of Exosome Sciences, Inc. 10% Promissory Note (3)
31.1	Certification of Principal Executive Officer pursuant to Securities Exchange Act rules 13a- 14(a) and 15d-14(a) as adopted pursuant to section 302 of the Sarbanes-Oxley Act of 2002*
31.2	Certification of Principal Financial Officer pursuant to Securities Exchange Act rules 13a- 14(a) and 15d-14(a) as adopted pursuant to section 302 of the Sarbanes-Oxley Act of 2002*
32.1	Certification of Principal Executive Officer pursuant to 18 U.S.C. section 1350, as adopted pursuant to section 906 of the Sarbanes-Oxley Act of 2002*
32.2	Certification of Principal Financial Officer pursuant to 18 U.S.C. section 1350, as adopted pursuant to section 906 of the Sarbanes-Oxley Act of 2002*

101.INS	XBRL Instance Document*
101.SCH	XBRL Schema Document*
101.CAL	XBRL Calculation Linkbase Document*
101.DEF	XBRL Definition Linkbase Document*
101.LAB	XBRL Label Linkbase Document*
101.PRE	XBRL Presentation Linkbase Document*

* Filed herewith.

(1) Incorporated by reference to the filing of such exhibit with the Company's Annual Report on Form 10-K for the year ended March 31, 2012.

(2) Incorporated by reference to the filing of such exhibit with the Company’s Quarterly Report on Form 10-Q for the period ended June 30, 2012.

(3) Incorporated by reference to the filing of such exhibit with the Company’s Current Report on Form 8-K filed on November 5, 2013.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

	AETHLON MEDICAL, INC.
Date: November 14, 2013	By: /s/ JAMES B. FRAKES JAMES B. FRAKES CHIEF FINANCIAL OFFICER CHIEF ACCOUNTING OFFICER