

APPLIED DNA SCIENCES INC  
Form 10QSB  
May 21, 2007

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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
FORM 10QSB

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

For the Quarterly period ended March 31, 2007

Commission file number 002-90519

**APPLIED DNA SCIENCES, INC.**  
(Exact name of registrant as specified in its charter)

**Nevada**  
(State or other jurisdiction of  
incorporation or organization)

**59-2262718**  
(I.R.S. Employer  
Identification Number)

**25 Health Sciences Drive, Suite 113**  
**Stony Brook, New York**  
(Address of Principal Executive Offices)

**11790**  
(Zip Code)

**(631) 444-6861**  
(Registrant's telephone number, including area code)

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

Yes  No

- Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

- The number of shares of Common Stock, \$0.001 par value, outstanding on May 15, 2007, was approximately 130,808,137 shares.

- Transitional Small Business Disclosure Format (check one):

Yes  No

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APPLIED DNA SCIENCES, INC  
**QUARTERLY REPORT ON FORM 10-QSB FOR THE  
QUARTERLY PERIOD ENDING MARCH 31, 2007**

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**PART I. FINANCIAL INFORMATION**

## ITEM 1. FINANCIAL STATEMENTS (UNAUDITED)

**APPLIED DNA SCIENCES, INC.**  
**(A Development stage company)**  
**CONDENSED CONSOLIDATED BALANCE SHEET**  
**(unaudited)**

		March 31, 2007
<b>ASSETS</b>		
Current assets:		
Cash	\$	89,232
Prepaid expenses		26,667
Total current assets		115,899
Property, plant and equipment-net of accumulated depreciation of \$51,800		136,561
Other assets:		
Deposits		13,822
Capitalized finance costs-net of accumulated amortization of \$1,413,563		271,537
Intangible assets:		
Patients, net of accumulated amortization of \$22,019 (Note B)		12,238
Intellectual property, net of accumulated amortization and write off of \$7,520,996 (Note B)		1,909,904
Total Assets	\$	2,459,961
<b>LIABILITIES AND DEFICIENCY IN STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable and accrued liabilities	\$	7,926,210
Convertible notes payable, net of unamortized discount (Note D)		4,930,894
Total current liabilities		12,857,104
Debt derivative and warrant liability		8,820,085
Commitments and contingencies (Note J)		
Deficiency in Stockholders' Equity- (Note F)		
Preferred stock, par value \$0.001 per share; 10,000,000 shares authorized; 60,000 issued and outstanding		6
Common stock, par value \$0.001 per share; 410,000,000 shares authorized; 121,162,385 issued		121,162

and outstanding (see Note J)		
Additional paid in capital		83,037,855
Accumulated deficit		(102,376,251)
Total deficiency in stockholders' equity		(19,217,228)

Total liabilities and Deficiency in Stockholders' Equity	\$	2,459,961
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See the accompanying notes to the consolidated financial statements

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**APPLIED DNA SCIENCES, INC.**  
**(A DEVELOPMENT STAGE COMPANY)**  
**CONDENSED CONSOLIDATED STATEMENTS OF LOSSES**  
**(unaudited)**

	For the three months Ended March 31,		For the six months Ended March 31,		From September 16, 2002 (Date of Inception) Through March 31, 2007
	2007	2006 RESTATED	2007	2006 RESTATED	
Sales	\$ -	\$ -	\$ -	\$ -	\$ 18,900
Cost of sales	-	-	-	-	15,639
Gross Profit	-	-	-	-	3,261
Operating expenses:					
Selling, general and administrative	1,988,931	949,634	4,043,386	2,794,311	84,109,344
Research and development	39,479	75,033	68,785	91,303	1,099,384
Impairment of intangible asset(s)	-	-	-	-	5,655,011
Depreciation and amortization	108,358	341,676	216,237	684,375	1,945,963
Total operating expenses	2,136,768	1,366,343	4,328,408	3,569,989	92,809,702
NET LOSS FROM OPERATIONS	(2,136,768)	(1,366,343)	(4,328,408)	(3,569,989)	(92,806,441)
Net gain (loss) in revaluation of debt derivative and warrant liabilities	(6,387,761)	3,967,870	(4,289,290)	10,756,660	29,256,537
Other income	-	3,520	977	9,493	111,807
Interest expense	(845,709)	(571,696)	(1,424,739)	(2,350,402)	(38,938,153)
Net income (loss) before provision for income taxes	(9,370,238)	2,033,351	(10,041,460)	4,845,762	(102,376,251)
Income taxes (benefit)	-	-	-	-	-
NET INCOME (LOSS)	\$ (9,370,238)	\$ 2,033,351	\$ (10,041,460)	\$ 4,845,762	\$ (102,376,251)
Net income (loss) per share-basic	\$ (0.08)	\$ 0.02	\$ (0.08)	\$ 0.04	

Net loss per share-assuming fully diluted-Note A		\$	(0.02)		\$	(0.03)
Weighted average shares outstanding-						
Basic	121,162,385		116,483,044	121,091,176		114,487,589
Fully diluted			119,483,044			117,487,589

See the accompanying notes to the consolidated financial  
statements

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APPLIED DNA SCIENCES, INC  
(A development stage company)  
CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDER'S EQUITY, (DEFICIENCY)  
FOR THE PERIOD SEPTEMBER 16, 2002 (DATE OF INCEPTION) THROUGH MARCH 31, 2007  
(unaudited)

	Preferred Preferred Shares Amount	Common Shares	Common Stock Amount	Additional Paid in Capital Amount	Common Stock Subscribed	Stock Subscription Receivable	Deficit Accumulated During Development Stage	Total
Issuance of common stock to Founders in exchange for services on September 16, 2002 at \$.01 per share	-	-	100,000	\$ 10	\$ 990	\$ -	\$ -	\$ 1,000
Net Loss	-	-	-	-	-	-	(11,612)	(11,612)
Balance at September 30, 2002	-	\$ -	100,000	\$ 10	\$ 990	\$ -	\$ (11,612)	\$ (10,612)
Issuance of common stock in connection with merger with Prohealth Medical Technologies, Inc on October 1, 2002	-	-	10,178,352	1,015	-	-	-	1,015
Cancellation of common stock in connection with merger with Prohealth Medical Technologies, Inc on October 21, 2002	-	-	(100,000)	(10)	(1,000)	-	-	(1,010)
Issuance of common stock in								

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exchange for services in October 2002 at \$0.65 per share	-	-	602,000	60	39,070	-	-	-	39,130
Issuance of common stock in exchange for subscription in November and December 2002 at \$0.065 per share	-	-	876,000	88	56,852	-	(56,940)	-	-
Cancellation of common stock in January 2003 previously issued in exchange for consulting services	-	-	(836,000)	(84)	(54,264)	-	54,340	-	(8)
Issuance of common stock in exchange for licensing services valued at \$0.065 per share in January 2003	-	-	1,500,000	150	97,350	-	-	-	97,500
Issuance of common stock in exchange for consulting services valued at \$0.13 per share in January 2003	-	-	586,250	58	76,155	-	-	-	76,213
Issuance of common stock in exchange for consulting services at \$0.065 per share in February 2003	-	-	9,000	1	584	-	-	-	585

Issuance of  
common stock to  
Founders in  
exchange for  
services valued  
at \$0.0001 per  
share in March  
2003

-	-	10,140,000	1,014	-	-	-	-	1,014
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APPLIED DNA SCIENCES, INC  
(A development stage company)  
CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDER'S EQUITY, (DEFICIENCY)  
FOR THE PERIOD SEPTEMBER 16, 2002 (DATE OF INCEPTION) THROUGH MARCH 31, 2007  
(unaudited)

	Preferred		Common	Common	Additional	Common	Stock	Deficit	
	Shares	Amount	Shares	Stock	Paid in	Stock	Subscribed	Accumulated	
	Shares	Amount	Shares	Amount	Capital	Subscribed	Receivable	During	Total
					Amount	Amount	Stage	Development	
Issuance of common stock in exchange for consulting services valued at \$2.50 per share in March 2003	-	-	91,060	10	230,624	-	-	-	230,634
Issuance of common stock in exchange for consulting services valued at \$0.065 per share in March 2003	-	-	6,000	1	389	-	-	-	390
Common stock subscribed in exchange for cash at \$1 per share in March 2003	-	-	-	-	18,000	-	-	-	18,000
Common stock issued in exchange for consulting services at \$0.065 per share on April 1, 2003	-	-	860,000	86	55,814	-	-	-	55,900
Common stock issued in exchange for cash at \$1.00 per									

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share on April 9, 2003	-	-	18,000	2	-	-	-	-	2
Common stock issued in exchange for consulting services at \$0.065 per share on April 9, 2003	-	-	9,000	1	584	-	-	-	585
Common stock issued in exchange for consulting services at \$2.50 per share on April 23, 2003	-	-	5,000	1	12,499	-	-	-	12,500
Common stock issued in exchange for consulting services at \$2.50 per share, on June 12, 2003	-	-	10,000	1	24,999	-	-	-	25,000
Common stock issued in exchange for cash at \$1.00 per share on June 17, 2003	-	-	50,000	5	49,995	-	-	-	50,000
Common stock subscribed in exchange for cash at \$2.50 per share pursuant to a private placement on June 27, 2003	-	-	-	-	-	24,000	-	-	24,000
Common stock retired in									

exchange for note payable at \$0.0118 per share, in June 30, 2003	-	-	(7,500,000)	(750)	750	-	-	-	-
Common stock issued in exchange for consulting services at \$0.065 per share, on June 30, 2003	-	-	270,000	27	17,523	-	-	-	17,550
Common stock subscribed in exchange for cash at \$1.00 per share pursuant to a private placement on June 30, 2003	-	-	-	-	-	10,000	-	-	10,000

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(unaudited)

	Preferred		Common	Additional	Common	Stock	Deficit		
	Shares	Amount	Shares	Paid in	Stock	Subscriptions	Accumulated	Development	Total
	Shares	Amount	Shares	Capital	Subscribed	Receivable	During	Stage	Total
Common stock subscribed in exchange for cash at \$2.50 per share pursuant to a private placement on June 30, 2003	-	-	-	-	24,000	-	-	-	24,000
Common stock issued in exchange for consulting services at approximately \$2.01 per share, July 2003	-	-	213,060	21	428,798	-	-	-	428,819
Common stock canceled in July 2003, previously issued for services rendered at \$2.50 per share	-	-	(24,000)	(2)	(59,998)	-	-	-	(60,000)
Common stock issued in exchange for options exercised at \$1.00 per share in July 2003	-	-	20,000	2	19,998	-	-	-	20,000
Common stock issued in exchange for exercise of									

options previously subscribed at \$1.00 per share in July 2003	-	-	10,000	1	9,999	(10,000)	-	-	-
Common stock issued in exchange for consulting services at approximately \$2.38 per Share in August 2003	-	-	172,500	17	410,915	-	-	-	410,932
Common stock issued in exchange for options exercised at \$1.00 per share in August 2003	-	-	29,000	3	28,997	-	-	-	29,000
Common stock issued in exchange for consulting services at approximately \$2.42 per share in September 2003	-	-	395,260	40	952,957	-	-	-	952,997
Common stock issued in exchange for cash at \$2.50 per share-subscription payable in September 2003	-	-	19,200	2	47,998	(48,000)	-	-	-
Common stock issued in exchange for cash at \$2.50 per share pursuant to a private placement in September 2003	-	-	6,400	1	15,999	-	-	-	16,000
Common stock issued in exchange for options exercised									



at \$1.00 per share in September 2003	-	-	95,000	10	94,991	-	-	-	95,001
Common stock subscription receivable reclassification adjustment	-	-	-	-	-	-	2,600	-	2,600
Common Stock subscribed to at \$2.50 per share in September 2003	-	-	-	-	-	300,000	-	-	300,000

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FOR THE PERIOD SEPTEMBER 16, 2002 (DATE OF INCEPTION) THROUGH MARCH 31, 2007  
(unaudited)

	Preferred		Common	Additional	Common	Deficit		
	Shares	Common	Stock	Paid in	Stock	Accumulated		
	Amount	Shares	Amount	Capital	Subscriptions	During		
	Shares			Amount	Receivable	Development		Total
					Stage			
Net Loss for the year ended September 30, 2003	-	-	-	-	-	-	(3,445,164)	(3,445,164)
Balance at September 30, 2003	- \$	- 17,811,082 \$	1,781 \$	2,577,568 \$	300,000 \$	- \$	(3,456,776)	(577,427)
Preferred shares issued in exchange for services at \$25.00 per share in October 2003	15,000	15	-	-	-	-	-	15
Common stock issued in exchange for consulting services at approximately \$2.85 per Share in October 2003	-	-	287,439	29	820,389	-	-	820,418
Common stock issued in exchange for cash at \$2.50 per share-subscription payable in October 2003	-	-	120,000	12	299,988	(300,000)	-	-
Common stock canceled in October 2003, previously issued								

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for services rendered at \$2.50 per share	-	-	(100,000)	(10)	(249,990)	-	-	-	(250,000)
Common stock issued in exchange for consulting services at approximately \$3 per share in November 2003	-	-	100,000	10	299,990	-	-	-	300,000
Common stock subscribed in exchange for cash at \$2.50 per share pursuant to a private placement in November, 2003	-	-	100,000	10	249,990	-	-	-	250,000
Common stock subscribed in exchange for cash at \$2.50 per share pursuant to a private placement in December, 2003	-	-	6,400	1	15,999	-	-	-	16,000
Common stock issued in exchange for consulting services at approximately \$2.59 per share in December 2003	-	-	2,125,500	213	5,504,737	-	-	-	5,504,950
Common Stock subscribed to at \$2.50 per share in December 2003	-	-	-	-	-	104,000	-	-	104,000
Beneficial conversion feature relating to notes payable	-	-	-	-	1,168,474	-	-	-	1,168,474

Beneficial conversion feature relating to warrants	-	-	-	-	206,526	-	-	-	206,526
Adjust common stock par value from \$0.0001 to \$0.50 per share, per amendment of articles dated in December 2004	-	-	-	10,223,166	(10,223,166)	-	-	-	-

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APPLIED DNA SCIENCES, INC  
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CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDER'S EQUITY, (DEFICIENCY)  
FOR THE PERIOD SEPTEMBER 16, 2002 (DATE OF INCEPTION) THROUGH MARCH 31, 2007  
(unaudited)

	Preferred Shares	Preferred Shares Amount	Common Shares	Common Stock Amount	Additional Paid in Capital Amount	Common Stock Subscribed	Common Stock Subscribed Receivable	Development Stage	Deficit Accumulated	Total
Common Stock issued pursuant to subscription at \$2.50 share in January 2004	-	-	41,600	20,800	83,200	(104,000)	-	-	-	-
Common stock issued in exchange for consulting services at \$2.95 per share in January 2004	-	-	13,040	6,520	31,948	-	-	-	-	38,468
Common stock issued in exchange for consulting services at \$2.60 per share in January 2004	-	-	123,000	61,500	258,300	-	-	-	-	319,800
Common stock issued in exchange for consulting services at \$3.05 per share in January 2004	-	-	1,000	500	2,550	-	-	-	-	3,050
Common stock issued in exchange for employee services at \$3.07 per share in February 2004	-	-	6,283	3,142	16,147	-	-	-	-	19,289

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Common stock issued in exchange for consulting services at \$3.04 per share in March 2004	-	-	44,740	22,370	113,640	-	-	-	136,010
Common Stock issued for options exercised at \$1.00 per share in March 2004	-	-	55,000	27,500	27,500	-	-	-	55,000
Common stock issued in exchange for employee services at \$3.00 per share in March 2004	-	-	5,443	2,722	13,623	-	-	-	16,345
Common stock issued in exchange for employee services at \$3.15 per share in March 2004	-	-	5,769	2,885	15,292	-	-	-	18,177
Preferred shared converted to common shares for consulting services at \$3.00 per share in March 2004	(5,000)	(5)	125,000	62,500	312,500	-	-	-	374,995
Common stock issued in exchange for employee services at \$3.03 per share in March 2004	-	-	8,806	4,400	22,238	-	-	-	26,638
Common Stock issued pursuant									

to subscription at \$2.50 per share in March 2004	-	-	22,500	11,250	(9,000)	-	-	-	2,250
Beneficial Conversion Feature relating to Notes Payable			-	-	122,362	-	-	-	122,362
Beneficial Conversion Feature relating to Warrants	-	-	-	-	177,638	-	-	-	177,638
Common stock issued in exchange for consulting services at \$2.58 per share in April 2004	-	-	9,860	4,930	20,511	-	-	-	25,441

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APPLIED DNA SCIENCES, INC  
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(unaudited)

	Preferred Shares	Preferred Shares Amount	Common Shares	Common Stock Amount	Additional Paid in Capital Amount	Common Stock Subscribed	Stock Subscription Receivable	Deficit Accumulated Development Stage	Total
Common stock issued in exchange for consulting services at \$2.35 per share in April 2004	-	-	11,712	5,856	21,667	-	-	-	27,523
Common stock issued in exchange for consulting services at \$1.50 per share in April 2004	-	-	367,500	183,750	367,500	-	-	-	551,250
Common stock returned to treasury at \$0.065 per share in April 2004	-	-	(50,000)	(25,000)	21,750	-	-	-	(3,250)
Preferred stock converted to common stock for consulting services at \$1.01 per share in May 2004	(4,000)	(4)	100,000	50,000	51,250	-	-	-	101,246
Common stock issued per subscription in May 2004	-	-	10,000	5,000	(4,000)	-	(1,000)	-	-



Common stock issued in exchange for consulting services at \$0.86 per share in May 2004	-	-	137,000	68,500	50,730	-	-	-	119,230
Common stock issued in exchange for consulting services at \$1.15 per share in May 2004	-	-	26,380	13,190	17,147	-	-	-	30,337
Common stock returned to treasury at \$0.065 per share in June 2004	-	-	(5,000)	(2,500)	2,175	-	-	-	(325)
Common stock issued in exchange for consulting services at \$0.67 per share in June 2004	-	-	270,500	135,250	45,310	-	-	-	180,560
Common stock issued in exchange for consulting services at \$0.89 per share in June 2004	-	-	8,000	4,000	3,120	-	-	-	7,120
Common stock issued in exchange for consulting services at \$0.65 per share in June 2004	-	-	50,000	25,000	7,250	-	-	-	32,250

Common stock issued pursuant to a private placement at \$1.00 per share in June 2004	-	-	250,000	125,000	125,000	-	-	-	250,000
Common stock issued in exchange for consulting services at \$0.54 per share in July 2004	-	-	100,000	50,000	4,000	-	-	-	54,000
Common stock issued in exchange for consulting services at \$0.72 per share in July 2004	-	-	5,000	2,500	1,100	-	-	-	3,600

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(unaudited)

	Preferred Shares	Preferred Amount	Common Shares	Common Stock Amount	Additional Paid in Capital	Common Stock Subscription Receivable	Deficit Accumulated Development Stage	Total
Common stock issued in exchange for consulting services at \$0.47 per share in July 2004	-	-	100,000	50,000	(2,749)	-	-	47,251
Common stock issued in exchange for consulting services at \$0.39 per share in August 2004	-	-	100,000	50,000	(11,000)	-	-	39,000
Preferred stock converted to common stock for consulting services at \$0.39 per share in August 2004	(2,000)	(2)	50,000	25,000	(5,500)	-	-	19,498
Common stock issued in exchange for consulting services at \$0.50 per share in August 2004	-	-	100,000	50,000	250	-	-	50,250
Common stock issued in								

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exchange for consulting services at \$0.56 per share in August 2004	-	-	200,000	100,000	12,500	-	-	-	112,500
Common stock issued in exchange for consulting services at \$0.41 per share in August 2004	-	-	92,500	46,250	(8,605)	-	-	-	37,645
Common stock issued in exchange for consulting services at \$0.52 per share in September 2004	-	-	1,000,000	500,000	17,500	-	-	-	517,500
Common stock issued in exchange for consulting services at \$0.46 per share in September 2004	-	-	5,000	2,500	(212)	-	-	-	2,288
Common stock issued pursuant to subscription at \$0.50 per share in September 2004	-	-	40,000	20,000	-	-	-	-	20,000
Preferred shares converted to common stock for consulting services at \$0.41 per share in September 2004	(4,000)	(4)	100,000	50,000	4,000	-	-	-	53,996
Preferred shares issued in									

exchange for service at \$25 per share in September 2004	60,000	6	-	-	1,499,994	-	-	-	1,500,000
Fair value of 2,841,000 warrants issued to non-employees and consultants for services rendered at approximately \$0.71 per warrant in September 2004	-	-	-	-	2,019,862	-	-	-	2,019,862
Net Loss Balance at September 30, 2004	-	-	-	-	-	-	-	(19,358,258)	(19,358,258)
	60,000	\$ 6	23,981,054	\$ 11,990,527	\$ 6,118,993	\$ -	\$ (1,000)	\$ (22,815,034)	\$ (4,706,508)

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FOR THE PERIOD SEPTEMBER 16, 2002 (DATE OF INCEPTION) THROUGH MARCH 31, 2007  
(unaudited)

	Preferred		Common	Common	Additional	Common	Stock	Deficit	
	Shares	Amount	Shares	Stock	Paid in	Stock	Subscribed	Accumulated	Total
	Shares	Amount	Shares	Amount	Capital	Subscribed	Receivable	Development	
	Shares	Amount	Shares	Amount	Amount	Subscribed	Receivable	Stage	Total
Common stock issued in exchange for consulting services at \$0.68 per share in October 2004	-	-	200,000	100,000	36,000	-	-	-	136,000
Common stock returned to treasury at \$0.60 per share in October 2004	-	-	(1,069,600)	(534,800)	(107,297)	-	-	-	(642,097)
Common stock issued in exchange for consulting services at \$0.60 per share in October 2004	-	-	82,500	41,250	8,250	-	-	-	49,500
Common Stock issued pursuant to subscription at \$0.60 per share in October 2004	-	-	500,000	250,000	50,000	(300,000)	-	-	-
Common stock issued in exchange for consulting services at \$0.50 per share in October 2004	-	-	532,500	266,250	-	-	-	-	266,250

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Common Stock issued in exchange for debt at \$0.50 per share in October 2004	-	-	500,000	250,000	-	-	-	-	250,000
Common Stock issued pursuant to subscription at \$0.45 per share in October 2004	-	-	1,000,000	500,000	(50,000)	(450,000)	-	-	-
Common stock issued in exchange for consulting services at \$0.45 per share in October 2004	-	-	315,000	157,500	(15,750)	-	-	-	141,750
Common Stock issued in exchange for consulting services at \$0.47 per share in November 2004	-	-	100,000	50,000	(3,000)	-	-	-	47,000
Common Stock issued in exchange for consulting services at \$0.80 per share in November 2004	-	-	300,000	150,000	90,000	-	-	-	240,000
Common Stock issued in exchange for consulting services at \$1.44 per share in November 2004	-	-	115,000	57,500	108,100	-	-	-	165,600

Common Stock issued in exchange for employee services at \$1.44 per share in November 2004	-	-	5,000	2,500	4,700	-	-	-	7,200
Warrants exercised at \$0.60 per share in November 2004	-	-	60,000	30,000	6,000	(4,000)	-	-	32,000
Beneficial Conversion discount relating to Notes Payable	-	-	-	-	1,465,000	-	-	-	1,465,000

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APPLIED DNA SCIENCES, INC  
(A development stage company)  
CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDER'S EQUITY, (DEFICIENCY)  
FOR THE PERIOD SEPTEMBER 16, 2002 (DATE OF INCEPTION) THROUGH MARCH 31, 2007  
(unaudited)

	Preferred Shares	Preferred Amount	Common Shares	Common Stock Amount	Additional Paid in Capital Amount	Common Stock Subscribed	Stock Subscriptions Receivable	Development Stage	Accumulated Deficit	Total
Common stock issued at \$0.016 per share in exchange for note payable in December 2004	-	-	5,500,000	2,750,000	(2,661,500)	-	-	-	-	88,500
Common stock issued in settlement of debt at \$0.50 per share in December 2004	-	-	2,930,000	1,465,000	-	(125,000)	-	-	-	1,340,000
Fair value of 6,063,500 warrants issued to non employees and consultants for services rendered at \$0.52 per warrant in October and December 2004	-	-	-	-	3,169,052	-	-	-	-	3,169,052
Warrants exercised at \$0.10 per share in January 2005	-	-	25,000	12,500	(10,000)	-	-	-	-	2,500
Common Stock issued in										

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settlement of debt at \$0.33 per share in January 2005	-	-	1,628,789	814,395	(276,895)	-	-	-	537,500
Warrants exercised at \$0.10 per share in January 2005	-	-	17,500	8,750	(7,000)	-	-	-	1,750
Common Stock issued in settlement of debt at \$0.33 per share in January 2005	-	-	2,399,012	1,199,504	(407,830)	-	-	-	791,674
Common Stock issued in exchange for consulting services at \$1.30 per share in January 2005	-	-	315,636	157,818	252,508	-	-	-	410,326
Fair value of warrant liability reclassified due to registration rights granted in February 2005	-	-	-	-	(3,108,851)	-	-	-	(3,108,851)
Common Stock issued in exchange for consulting services at \$1.44 per share in February 2005	-	-	5,796,785	2,898,393	5,418,814	-	-	-	8,317,207
Fair value of 55,000 warrants issued to consultants for services at \$1.31									

per warrant in February 2005	-	-	-	-	72,017	-	-	-	72,017
Common Stock issued in settlement of debt at \$0.33 per share in February 2005	-	-	75,757	37,879	(12,879)	-	-	-	25,000
Warrants exercised at \$0.10 per share in February 2005	-	-	20,000	10,000	(8,000)	-	-	-	2,000
Common Stock issued in settlement of debt at \$0.33 per share in February 2005	-	-	606,060	303,030	(103,030)	-	-	-	200,000
Warrants exercised at \$0.10 per share in February 2005	-	-	45,000	22,500	(18,000)	-	-	-	4,500

APPLIED DNA SCIENCES, INC  
(A development stage company)  
CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDER'S EQUITY, (DEFICIENCY)  
FOR THE PERIOD SEPTEMBER 16, 2002 (DATE OF INCEPTION) THROUGH MARCH 31, 2007  
(unaudited)

	Preferred Shares	Preferred Shares Amount	Common Shares	Common Stock Amount	Additional Paid in Capital Amount	Common Stock Subscribed	Common Stock Subscribable	Deficit Accumulated Development Stage	Total
Common Stock issued in exchange for related party debt at \$1.31 per share in February 2005	-	-	1,500,000	750,000	1,215,000	-	-	-	1,965,000
Common Stock issued in settlement of debt at \$0.33 per share in February 2005	-	-	278,433	139,217	(47,334)	-	-	-	91,883
Common Stock issued in exchange for consulting services at \$1.17 per share in February 2005	-	-	17,236	8,618	11,548	-	-	-	20,166
Common stock issued in exchange for debt at \$0.50 per share in February 2005	-	-	300,000	150,000	-	-	-	-	150,000
Common Stock issued in exchange for consulting services at \$0.95 per share	-	-	-	-	-	-	-	-	-

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in February 2005	-	-	716,500	358,250	322,425	-	-	-	680,675
Common Stock issued in exchange for consulting services at \$0.95 per share in February 2005	-	-	10,500	5,250	4,725	-	-	-	9,975
Common stock issued in exchange for debt at \$0.50 per share in March 2005	-	-	13,202,000	6,601,000	-	-	-	-	6,601,000
Common Stock issued in exchange for consulting services at \$1.19 per share in March 2005	-	-	185,000	92,500	127,650	-	-	-	220,150
Options exercised at \$0.60 per share in March 2005	-	-	100,000	50,000	10,000	-	-	-	60,000
Common Stock issued in exchange for consulting services at \$0.98 per share in March 2005	-	-	1,675,272	837,636	804,131	-	-	-	1,641,767
Common Stock issued in exchange for consulting services at \$0.92 per share in March 2005	-	-	24,333	12,167	10,219	-	-	-	22,386
Common Stock issued in									

exchange for consulting services at \$0.99 per share in March 2005	-	-	15,000	7,500	7,350	-	-	-	14,850
Common stock issued in exchange for debt at \$0.50 per share in March 2005	-	-	1,240,000	620,000	-	-	-	-	620,000

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APPLIED DNA SCIENCES, INC  
(A development stage company)  
CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDER'S EQUITY, (DEFICIENCY)  
FOR THE PERIOD SEPTEMBER 16, 2002 (DATE OF INCEPTION) THROUGH MARCH 31, 2007  
(unaudited)

	Preferred Shares	Preferred Amount	Common Shares	Common Stock Amount	Additional Paid in Capital Amount	Common Stock Subscribed	Stock Subscriptions Receivable	Development Stage	Accumulated Deficit	Total
Common stock canceled for shares issued in exchange of debt in March 2005	-	-	(500,000)	(250,000)	-	-	-	-	-	(250,000)
Common stock subscribed canceled in March 2005	-	-	-	-	-	750,000	-	-	-	750,000
Common Stock issued in exchange for consulting services at \$0.89 per share in March 2005	-	-	10,000	5,000	3,900	-	-	-	-	8,900
Adjust common stock par value from \$0.50 to \$0.001 per share, per amendment of Articles of Incorporation in March-05	-	-	-	(32,312,879)	32,312,879	-	-	-	-	-
Beneficial Conversion discount relating to Notes Payable in March 2005	-	-	-	-	7,371,000	-	-	-	-	7,371,000
Stock options granted to employees in exchange for										

services rendered, at exercise price below fair value of common stock in March 2005	-	-	-	-	180,000	-	-	-	180,000
Common Stock issued in exchange for consulting services at \$0.80 per share in April 2005	-	-	160,000	160	127,840	-	-	-	128,000
Common Stock issued in exchange for consulting services at \$0.80 per share in April 2005	-	-	40,000	40	31,960	-	-	-	32,000
Common Stock issued in exchange for consulting services at \$0.75 per share in April 2005	-	-	850,000	850	636,650	-	-	-	637,500
Common Stock issued in exchange for consulting services at \$0.33 per share in April 2005	-	-	500,000	500	164,500	-	-	-	165,000
Common Stock canceled during April 2005, previously issued for									



services rendered at \$3.42 per share	-	-	(10,000)	(10)	(34,190)	-	-	-	(34,200)
Common Stock issued in settlement of debt at \$0.33 per share in April 2005	-	-	75,758	77	24,923	(25,000)	-	-	-
Common Stock issued in exchange for consulting services at \$0.68 per share in April 2005	-	-	50,000	50	33,950	-	-	-	34,000
Proceeds received against subscription payable in June 2005	-	-	-	-	-	118,000	-	-	118,000

APPLIED DNA SCIENCES, INC  
(A development stage company)  
CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDER'S EQUITY, (DEFICIENCY)  
FOR THE PERIOD SEPTEMBER 16, 2002 (DATE OF INCEPTION) THROUGH MARCH 31, 2007  
(unaudited)

	Preferred		Common	Common	Additional	Common	Stock	Deficit	
	Shares	Amount	Shares	Stock	Paid in	Stock	Subscriptions	Accumulated	
	Shares	Amount	Shares	Amount	Capital	Subscribed	Receivable	Development	Total
Common Stock canceled in June 2005, previously issued for services rendered at \$0.50 per share	-	-	(10,000)	(10)	(4,990)	-	-	-	(5,000)
Cancellation of previously granted stock options granted to employees for services rendered, at exercise price below fair value of common stock	-	-	-	-	(180,000)	-	-	-	(180,000)
Common Stock issued in exchange for consulting services at \$0.60 per share in July 2005	-	-	157,000	157	94,043	-	-	-	94,200
Common Stock issued in exchange for intellectual property at \$0.67 per share in July 2005	-	-	36,000,000	36,000	24,084,000	-	-	-	24,120,000

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Common Stock issued in exchange for consulting services at \$0.60 per share in July 2005	-	-	640,000	640	383,360	-	-	-	384,000
Common Stock issued in exchange for employee services at \$0.48 per share in July 2005	-	-	8,000,000	8,000	3,832,000	-	-	-	3,840,000
Common Stock issued in exchange for consulting services at \$0.94 per share in July 2005	-	-	121,985	121	168,217	-	-	-	168,338
Common Stock issued in exchange for consulting services at \$0.48 per share in August 2005	-	-	250,000	250	119,750	-	-	-	120,000
Common Stock penalty shares issued pursuant to pending SB-2 registration at \$0.62 per share in September 2005	-	-	814,158	814	501,858	-	-	-	502,672
Common Stock penalty shares issued pursuant to pending SB-2 registration at \$0.70 per share in September 2005	-	-	391,224	391	273,466	-	-	-	273,857

Common Stock  
issued in  
exchange for  
consulting  
services at \$0.94  
per share  
in September  
2005

-	-	185,000	185	173,715	-	-	-	173,900
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Common Stock  
returned in  
September  
2005,  
previously  
issued for  
services  
rendered at  
\$0.40 per share

-	-	(740,000)	(740)	(453,232)	56,000	1,000	-	(396,972)
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APPLIED DNA SCIENCES, INC  
(A development stage company)  
CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDER'S EQUITY, (DEFICIENCY)  
FOR THE PERIOD SEPTEMBER 16, 2002 (DATE OF INCEPTION) THROUGH MARCH 31, 2007  
(unaudited)

	Preferred Shares	Preferred Amount	Common Shares	Common Stock Amount	Additional Paid in Capital Amount	Common Stock Subscriptions Receivable	Common Stock Development Stage	Deficit Accumulated	Total
Net Loss	-	-	-	-	-	-	-	(67,109,519)	(67,109,519)
Balance as of September 30, 2005	60,000	\$ 6	112,230,392	\$ 112,230	\$ 82,320,715	\$ 20,000	\$ -	\$ (89,924,553)	\$ (7,471,602)
Common stock issued in exchange for services at \$0.50 per share in October 2005	-	-	400,000	400	199,600	-	-	-	200,000
Common Stock issued in exchange for consulting services at \$0.75 per share in October 2005	-	-	100,000	100	74,900	-	-	-	75,000
Common Stock returned in October 2005, previously issued for services rendered at \$0.60 per share	-	-	(350,000)	(350)	(209,650)	-	-	-	(210,000)
Common stock issued pursuant									

to subscription at \$0.50 per share in December 2005	-	-	40,000	40	19,960	(20,000)	-	-	-
Common Stock issued to investors pursuant to registration rights agreement at \$0.51 per share in December 2005	-	-	505,854	506	257,480	-	-	-	257,986
Common Stock returned in January 2006, previously issued for services rendered at \$0.60 per share	-	-	(250,000)	(250)	(149,750)	-	-	-	(150,000)
Common Stock issued to investors pursuant to registration rights agreement at \$0.32 per share in January 2006	-	-	806,212	806	257,182	-	-	-	257,988
Common Stock issued to investors pursuant to registration rights agreement at \$0.20 per share									

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in January 2006	-	-	1,289,927	1,290	256,695	-	-	-	257,985
Fair value of 200,000 warrants issued to consultants for services at \$0.22 per warrant in January 2006	-	-	-	-	43,098	-	-	-	43,098
Common Stock issued in exchange for consulting services at \$0.17 per share in February 2006	-	-	160,000	160	27,040	-	-	-	27,200
Common Stock issued in exchange for consulting services at \$0.16 per share in February 2006	-	-	3,800,000	3,800	604,200	-	-	-	608,000
Common Stock returned in March 2006, previously issued for services rendered at \$0.80 per share	-	-	(150,000)	(150)	(119,850)	-	-	-	(120,000)

APPLIED DNA SCIENCES, INC  
(A development stage company)  
CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDER'S EQUITY, (DEFICIENCY)  
FOR THE PERIOD SEPTEMBER 16, 2002 (DATE OF INCEPTION) THROUGH MARCH 31, 2007  
(unaudited)

	Preferred Shares	Preferred Shares Amount	Common Shares	Common Stock Amount	Additional Paid in Capital Amount	Common Stock Subscriptions	Common Stock Redivible	Deficit Accumulated Development Stage	Total
Previously issued warrants reclassified to warrant liability	-	-	-	-	(1,584,614)	-	-	-	(1,584,614)
Common Stock issued in exchange for consulting services at \$0.20 per share in July 2006	-	-	2,400,000	2,400	477,600	-	-	-	480,000
Fair value of stock options granted to employees in exchange for services rendered in September 2006	-	-	-	-	153,000	-	-	-	153,000
Net loss	-	-	-	-	-	-	-	(2,410,237)	(2,410,237)
Balance as of September 30, 2006	60,000	\$ 6	\$ 120,982,385	\$ 120,982	\$ 82,627,606	\$ -	\$ -	(92,334,791)	\$ (9,586,197)
Common stock issued in Dec 2006 in settlement of related party debt									



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at \$2.28 per share	-	-	180,000	180	410,249	-	-	-	410,429
Net loss	-	-	-	-	-	-	-	(10,041,460)	(10,041,460)
Balance as of March 31, 2007	60,000	\$ 6	121,162,385	\$ 121,162	\$ 83,037,855	\$ -	\$ -	\$ (102,376,251)	\$ (19,217,228)

See accompanying notes to consolidated financial statements

**APPLIED DNA SCIENCES, INC**  
**(A DEVELOPMENT STAGE COMPANY)**  
**CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS**  
**(unaudited)**

	For the six months ended March 31,		For the Period
	2007	2006	September 16,
		RESTATED	2002
			(Date of
			Inception)
			through
			March 31, 2007
Cash flows from operating activities:			
Net income (loss)	\$ (10,041,460)	\$ 4,845,762	\$ (102,376,251)
Adjustments to reconcile net loss to net used in operating activities:			
Depreciation and amortization	216,237	684,375	1,945,963
Organization expenses	-	-	88,500
Impairment of intangible assets	-	-	5,655,011
Preferred shares issued in exchange for services	-	-	1,500,000
Options and warrants issued in exchange for services rendered	-	43,100	11,001,255
Income attributable to repricing of warrants and debt derivatives	4,289,290	(10,756,660)	(29,256,538)
Financing costs attributable to issuance of warrants	-	2,271,000	25,419,214
Amortization of beneficial conversion feature-convertible notes	-	-	10,461,000
Amortization of capitalized financing costs	777,550	-	1,413,563
Amortization of debt discount attributable to convertible debentures	1,169,123	35,390	1,900,613
Debt in exchange for common stock at fair market price	-	-	1,365,000
Common stock issued in exchange for services rendered	-	710,200	31,964,573
Common stock exchanged for intellectual property in connection with costs of acquiring intangible assets	-	-	14,689,100
Common stock issued in connection with penalties pursuant to registration	-	773,958	1,550,487
Common stock canceled-previously issued for services rendered	-	(480,000)	(1,343,845)
Change in assets and liabilities:			
Decrease (increase) in accounts receivable	18,050	9,301	-
Decrease (increase) in prepaid expenses and deposits	80,000	-	(40,929)
Decrease (increase) in other assets	-	(9,120)	(13,450)
Increase in due related parties	-	2,496	40,753
Increase (decrease) in accounts payable and accrued liabilities	2,366,177	742,575	7,291,787
Net cash used in operating activities	(1,125,033)	(1,127,623)	(16,744,194)

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Cash flows from investing activities:

Payments for patent filing	-	-	(25,698)
Acquisition (disposal) of property and equipment, net	(11,039)	(35,852)	(188,360)
Net cash provided by (used in) investing activities	(11,039)	(35,852)	(214,058)

Cash flows from financing activities:

Proceeds from sale of common stock, net of cost	-	-	432,000
Proceeds from issuance of convertible notes	-	1,210,000	13,446,500
Proceeds from sale of options	-	-	343,750
Repayment of debt	-	-	(24,854)
Proceeds from loans	-	-	2,750,000
Advances from shareholders	-	-	100,088
Net cash provided by financing activities	-	1,210,000	17,047,484

Net increase in cash and cash equivalents	(1,136,072)	46,525	89,232
Cash and cash equivalents at beginning of period	1,225,304	31,190	-
Cash and cash equivalents at end of period	\$ 89,232	\$ 77,715	\$ 89,232

**APPLIED DNA SCIENCES, INC**  
**(A DEVELOPMENT STAGE COMPANY)**  
**CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS**  
**(unaudited)**

	For the six months ended March 31,		For the Period
	2007	2006	September 16, 2002 (Date of Inception) through March 31, 2007
Supplemental Disclosures of Cash Flow Information:			
Cash paid during period for interest	-	-	-
Cash paid during period for taxes	-	-	-
Non-cash transactions:			
Common stock issued for services	-	710,200	31,964,573
Common stock issued in exchange for intellectual property	-	-	
Common stock issued in exchange for previously incurred debt	16,200	-	2,313,500
Common stock canceled-previously issued for services rendered	-	(480,000)	(1,343,845)
Common stock issued for ESOP shares	-	-	
Common stock penalty shares issued pursuant to Pending SB-2 registration	-	773,958	
Amortization of beneficial conversion feature	-	-	10,461,000
Preferred shares in exchange for service at \$25 per share in September 2004	-	-	1,500,000
Fair value of options and warrants issued to consultants for services	-	43,100	11,001,255
Acquisition:			
Common stock retained	-	-	1,015
Assets acquired	-	-	(135)
Total consideration paid	-	-	880
Organizational expenses-note issued in exchange for shares retired			88,500
Common stock issued in exchange for note payable			88,500

See the accompanying notes to the consolidated financial statements

**APPLIED DNA SCIENCES, INC**  
**(a development stage company)**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**MARCH 31, 2007**  
**(Unaudited)**

**NOTE A - SUMMARY OF ACCOUNTING POLICIES**

*General*

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with the instructions to Form 10-QSB, and therefore, do not include all the information necessary for a fair presentation of financial position, results of operations and cash flows in conformity with generally accepted accounting principles.

In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three and six month period ended March 31, 2007 are not necessarily indicative of the results that may be expected for the fiscal year ending September 30, 2007. The unaudited condensed consolidated financial statements should be read in conjunction with the consolidated September 30, 2006 financial statements and footnotes thereto included in the Company's SEC Form 10-KSB, as amended.

*Business and Basis of Presentation*

On September 16, 2002, Applied DNA Sciences, Inc. (the "Company") was incorporated under the laws of the State of Nevada. The Company is in the development stage, as defined by Statement of Financial Accounting Standards No. 7 ("SFAS No. 7") and its efforts have been principally devoted to developing DNA embedded biotechnology security solutions in the United States. To date, the Company has generated nominal sales revenues, has incurred expenses and has sustained losses. Consequently, its operations are subject to all the risks inherent in the establishment of a new business enterprise. For the period from inception through March 31, 2007, the Company has accumulated losses of \$102,376,251.

In March 2007, the Company purchased all the outstanding shares of Applied DNA Sciences Europe Limited, an English limited company, as a wholly owned subsidiary, for a purchase price of \$10,000. In conjunction with the acquisition, the Company acquired the rights to sell products and services in the United Kingdom. Included as part of the acquisition agreement, the Company is obligated to pay a 2% fee of any United Kingdom sales to the former shareholder of Applied DNA Sciences Europe Limited for one year commencing with the first product/services sales. The cost of acquisition was charged to current period operating expenses.

The consolidated financial statements include the accounts of the Company, and its wholly-owned subsidiaries, Applied DNA Operations Management, Inc., APDN (B.V.I.) Inc. and Applied DNA Sciences Europe Limited. Significant inter-company transactions have been eliminated in consolidation.

*Reclassification*

Certain prior period amounts have been reclassified for comparative purposes.

*Property and Equipment*

Property and equipment are stated at cost and depreciated over their estimated useful lives of 3 to 5 years using the straight line method. At March 31, 2007 property and equipment consist of:

Computer equipment \$ 27,404

Lab equipment	54,973
Furniture	105,984
Accumulated depreciation	(51,800)
Net	\$ 136,561

**APPLIED DNA SCIENCES, INC**  
**(a development stage company)**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**MARCH 31, 2007**  
**(Unaudited)**

**NOTE A - SUMMARY OF ACCOUNTING POLICIES (continued)**

*Stock Based Compensation*

In December 2002, the FASB issued SFAS No. 148, "Accounting for Stock-Based Compensation-Transition and Disclosure-an amendment of SFAS 123." This statement amends SFAS No. 123, "Accounting for Stock-Based Compensation," to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. In addition, this statement amends the disclosure requirements of SFAS No. 123 to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based employee compensation and the effect of the method used on reported results. The Company has chosen to continue to account for stock-based compensation using the intrinsic value method prescribed in APB Opinion No. 25 and related interpretations. Accordingly, compensation expense for stock options is measured as the excess, if any, of the fair market value of the Company's stock at the date of the grant over the exercise price of the related option. The Company has adopted the annual disclosure provisions of SFAS No. 148 in its financial reports for the year ended September 30, 2006 and for the subsequent periods. The Company did not issue employee options as stock-based compensation during the three or six months ended March 31, 2007 and therefore has no unrecognized stock compensation related liabilities ended March 31, 2007.

On January 1, 2006, the Company adopted the fair value recognition provisions of Financial Accounting Standards Board ("FASB") Statement of Financial Accounting Standards ("SFAS") No. 123, Accounting for Stock Based Compensation, to account for compensation costs under our stock option plans. We previously utilized the intrinsic value method under Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees (as amended) ("APB 25"). Under the intrinsic value method prescribed by APB 25, no compensation costs were recognized for our employee stock options because the option exercise price equaled the market price on the date of the grant. Prior to January 1, 2006 we only disclosed the pro forma effects on net income and earnings per share as if the fair value recognition provisions of SFAS 123(R) had been utilized.

In adopting SFAS No. 123(R), we elected to use the modified prospective method to account for the transition from the intrinsic value method to the fair value recognition method. Under modified prospective method, compensation cost is recognized from the adoption date forward for all new stock options granted and for any outstanding unvested awards as if the fair value method had been applied to those awards as of the date of the grant. In the six months ended March 31, 2007; the Company did not grant any employee stock options.

*Revenue Recognition*

Revenues are recognized in the period that services are provided. For revenue from product sales, the Company recognizes revenue in accordance with Staff Accounting Bulletin No. 104, REVENUE RECOGNITION ("SAB104"), which superseded Staff Accounting Bulletin No. 101, REVENUE RECOGNITION IN FINANCIAL STATEMENTS ("SAB101"). SAB 101 requires that four basic criteria must be met before revenue can be recognized: (1) persuasive evidence of an arrangement exists; (2) delivery has occurred; (3) the selling price is fixed and determinable; and (4) collectibility is reasonably assured. Determination of criteria (3) and (4) are based on management's judgments regarding the fixed nature of the selling prices of the products delivered and the collectibility of those amounts. Provisions for discounts and rebates to customers, estimated returns and allowances, and other adjustments are provided for in the same period the related sales are recorded. The Company defers any revenue for which the product

has not been delivered or is subject to refund until such time that the Company and the customer jointly determine that the product has been delivered or no refund will be required. At March 31, 2007 the Company did not have any deferred revenue.

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**NOTE A - SUMMARY OF ACCOUNTING POLICIES (continued)**

SAB 104 incorporates Emerging Issues Task Force 00-21 (“EITF 00-21”), MULTIPLE DELIVERABLE REVENUE ARRANGEMENTS. EITF 00-21 addresses accounting for arrangements that may involve the delivery or performance of multiple products, services and/or rights to use assets. The effect of implementing EITF 00-21 on the Company’s financial position and results of operations was not significant.

*Concentrations of Credit Risk*

Financial instruments and related items which potentially subject the Company to concentrations of credit risk consist primarily of cash, cash equivalents and trade receivables. The Company places its cash and temporary cash investments with credit quality institutions. At times, such investments may be in excess of the FDIC insurance limit. The Company periodically reviews its trade receivables in determining its allowance for doubtful accounts. At March 31, 2007, allowance for doubtful receivable was \$0.

Net income (loss) per share

The following reconciliation of net income and share amounts used in the computation of income (loss) per share for the three and six months ended March 31, 2006:

	Three Months Ended March 31, 2006	Six Months Ended March 31, 2006
Net income used in computing basic net income per share	\$ 2,033,351	\$ 4,845,762
Impact of assumed assumptions:		
Fair value of warrants relating to convertible debt charged to interest expense		1,758,900
Impact of equity classified as liability:		
Gain on warrant liability marked to fair value	(3,967,870)	(10,756,660)
Net loss in computing diluted net loss per share:	\$ (1,934,519)	\$ (4,151,998)

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**NOTE A - SUMMARY OF ACCOUNTING POLICIES (continued)**

The weighted average shares outstanding used in the basic net income per share computations for the three and six months ended March 31, 2006 was 116,483,044 and 114,487,589, respectively. In determining the number of shares used in computing diluted loss per share, the Company added approximately 3,000,000 potentially dilutive securities for the three and six months ended March 31, 2006. The potentially dilutive securities added were mostly attributable to the warrants, options and convertible debentures outstanding. As a result, the diluted loss per share for the three and six months ended March 31, 2006 was \$0.02 and \$0.03, respectively.

*Derivative Financial Instruments*

The Company's derivative financial instruments consist of embedded derivatives related to the 10% Secured Convertible Promissory Notes (the "Serial Notes") issued in 2006 (see Note D). These embedded derivatives include certain conversion features, variable interest features, call options and default provisions. The accounting treatment of derivative financial instruments requires that the Company recorded the derivatives and related warrants at their fair values as of the inception date of the Note Agreement (estimated at \$2,419,719) and at fair value as of each subsequent balance sheet date. In addition, under the provisions of EITF Issue No. 00-19, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock," as a result of entering into the Notes, the Company is required to classify all other non-employee stock options and warrants as derivative liabilities and mark them to market at each reporting date. The fair value of such options and warrants that were reclassified as liabilities from additional paid-in capital in the six months ended March 31, 2007 totaled \$1,584,614. Any change in fair value will be recorded as non-operating, non-cash income or expense at each reporting date. If the fair value of the derivatives is higher at the subsequent balance sheet date, the Company will record a non-operating, non-cash charge. If the fair value of the derivatives is lower at the subsequent balance sheet date, the Company will record non-operating, non-cash income. Conversion-related derivatives were valued using the Binomial Option Pricing Model with the following assumptions: dividend yield of 0%; annual volatility of 111 to 112%; and risk free interest rate of 4.96 to 5.15% as well as probability analysis related to trading volume restrictions. The remaining derivatives were valued using discounted cash flows and probability analysis. The derivatives are classified as long-term liabilities (see Note F).

*New Accounting Pronouncements*

In February 2006, the FASB issued SFAS No. 155. "Accounting for certain Hybrid Financial Instruments an amendment of FASB Statements No. 133 and 140," or SFAS No. 155. SFAS No. 155 permits fair value remeasurement for any hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation, clarifies which interest-only strips and principal-only strips are not subject to the requirements of Statement No. 133, establishes a requirement to evaluate interests in securitized financial assets to identify interests that are freestanding derivatives or that are hybrid financial instruments that contain an embedded derivative requiring bifurcation, clarifies that concentrations of credit risk in the form of subordination are not embedded derivatives, and amends SFAS No. 140 to eliminate the prohibition on a qualifying special purpose entity from holding a derivative financial instrument that pertains to a beneficial interest other than another derivative financial instrument. SFAS 155 is effective for all financial instruments acquired or issued after the beginning of an entity's first fiscal year that begins after September 15, 2006. We do not expect the adoption of SFAS 155 to have a material impact on our consolidated financial position, results of operations or cash flows.



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**NOTE A - SUMMARY OF ACCOUNTING POLICIES (continued)**

In March 2006, the FASB issued FASB Statement No. 156, Accounting for Servicing of Financial Assets - an amendment to FASB Statement No. 140. Statement 156 requires that an entity recognize a servicing asset or servicing liability each time it undertakes an obligation to service a financial asset by entering into a service contract under certain situations. The new standard is effective for fiscal years beginning after September 15, 2006. The adoption of SFAS No.156 did not have a material impact on the Company's financial position and results of operations.

In July 2006, the FASB issued Interpretation No. 48 (FIN 48). "*Accounting for uncertainty in Income Taxes*". FIN 48 clarifies the accounting for Income Taxes by prescribing the minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. It also provides guidance on derecognition, measurement, classification, interest and penalties, accounting in interim periods, disclosure and transition and clearly scopes income taxes out of SFAS 5, "*Accounting for Contingencies*". FIN 48 is effective for fiscal years beginning after December 15, 2006. We have not yet evaluated the impact of adopting FIN 48 on our consolidated financial position, results of operations and cash flows.

In September 2006 the Financial Account Standards Board (the "FASB") issued its Statement of Financial Accounting Standards 157, Fair Value Measurements. This Statement defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles (GAAP), and expands disclosures about fair value measurements. This Statement applies under other accounting pronouncements that require or permit fair value measurements, the Board having previously concluded in those accounting pronouncements that fair value is the relevant measurement attribute. Accordingly, this Statement does not require any new fair value measurements. However, for some entities, the application of this Statement will change current practice. FAS 157 effective date is for fiscal years beginning after November 15, 2007. The Company does not expect adoption of this standard will have a material impact on its financial position, operations or cash flows.

In September 2006 the FASB issued its Statement of Financial Accounting Standards 158 "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans". This Statement improves financial reporting by requiring an employer to recognize the overfunded or underfunded status of a defined benefit postretirement plan (other than a multiemployer plan) as an asset or liability in its statement of financial position and to recognize changes in that funded status in the year in which the changes occur through comprehensive income of a business entity or changes in unrestricted net assets of a not-for-profit organization. This Statement also improves financial reporting by requiring an employer to measure the funded status of a plan as of the date of its year-end statement of financial position, with limited exceptions. The effective date for an employer with publicly traded equity securities is as of the end of the fiscal year ending after December 15, 2006. The Company does not expect adoption of this standard will have a material impact on its financial position, operations or cash flows.

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities." SFAS 159 permits entities to choose to measure many financial instruments, and certain other items, at fair value. SFAS 159 applies to reporting periods beginning after November 15, 2007. The adoption of SFAS 159 is not expected to have a material impact on the Company's financial condition or results of operations

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**NOTE B - INTANGIBLE ASSETS AND AMORTIZATION**

The Company has adopted SFAS No. 142, Goodwill and Other Intangible Assets, whereby the Company periodically test its intangible assets for impairment. On an annual basis, and when there is reason to suspect that their values have been diminished or impaired, these assets are tested for impairment, and write-downs will be included in results from operations.

Biowell Technology, Inc.

On July 12, 2005, the Company acquired certain intellectual properties from Biowell Technology, Inc. ("Biowell") through an Asset Purchase Agreement ("Agreement") in exchange for 36 million shares of the Company's restricted common stock having an aggregate fair value at the date of issuance of \$24,120,000. The intangible assets acquired consist of proprietary DNA anti-counterfeit trade secrets created by Biowell that are intended to protect intellectual property from counterfeiting, fraud, piracy, product diversion and unauthorized intrusion.

The purchase price has been allocated as follows:

Amortizable intangible assets acquired are comprised of:

Developed core technologies	\$	2,260,900
Developed product technologies		7,170,000
Total amortizable intangible assets		9,430,900
Transaction costs		14,869,100
Total purchase price	\$	24,120,000

In Process Research & Development

The Company concluded as of the date of acquisition, the acquired intangible assets, consisting of developed core and product technologies had reached full development and that it was not the intention of the Company's management to utilize the asset in specific research and development activities as defined in SFAS No. 2 Accounting for Research & Development Costs. As a result, the Company determined there was no in-process research and development ("IPR&D") projects in place related to the technology acquired, nor any future research and development activities planned. Accordingly, there is no charge to operations during the year ended September 30, 2005 for IPR&D in connection with the acquisition of the assets.

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**NOTE B - INTANGIBLE ASSETS AND AMORTIZATION (continued)***Transaction costs*

The amount of the purchase price that could not be allocated to acquire identifiable intangible assets or IPR & D was \$14,689,100 and was charged to operations as a cost of the transaction during the year ended September 30, 2005.

The identifiable intangible assets acquired and their carrying value at March 31, 2007 are:

Trade secrets and developed technologies (Weighted average life of 7 years)	\$ 9,430,900
Patents (Weighted average life of 5 years)	34,257
Total Amortized identifiable intangible assets-Gross carrying value:	\$ 9,465,157
Less:	
Accumulated Amortization	(1,888,004)
Impairment	(5,655,011)
Net:	\$ 1,922,142
Residual value:	\$ 0

Total amortization expense charged to operations for the three and six months ended March 31, 2007 was \$92,661 and \$185,322, respectively. Amortization expense charged to operations for the three and six months ended March 31, 2006 was \$338,545 and \$667,090 respectively.

Estimated amortization expense as of March 31, 2007 is as follows:

2007	\$ 370,642
2008	370,642
2009	365,504
2010	363,791
2011 and thereafter	451,563

Total \$ 1,922,142

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**NOTE C - PRIVATE PLACEMENT OF CONVERTIBLE NOTES**

Convertible notes payable as of March 31, 2007 are as follows:

10% Secured Convertible Notes Payable dated March 8, 2006, net of unamortized debt discount of \$250,810 (see below)	\$ 1,249,190
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10% Secured Convertible Notes Payable dated May 2, 2006, net of unamortized debt discount of \$37,997 (see below)	962,003
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10% Secured Convertible Notes Payable dated June 15, 2006, net of unamortized debt discount of \$230,299 (see below)	2,719,701 4,930,894
Less: current portion	(4,930,894) \$ -

10% Secured Convertible Promissory Notes dated March 8, 2006

On March 8, 2006, in connection with a private placement, the Company issued 10% Secured Convertible Promissory Notes in the aggregate principal amount of \$1,500,000 (the "Serial Notes") and warrants to purchase 3,000,000 shares of the Company's common stock to accredited investors. The Serial Notes bear interest at 10%, mature on September 7, 2007 and are convertible into the Company's common stock, at the holder's option, at fifty cents (\$.50) per share during the period from the date of issuance (March 8, 2006) through March 7, 2007. Should the holder of the Serial Note elect not to convert to the Company's common stock on or before March 7, 2007, the outstanding principal, along with accrued and unpaid interest automatically converts to the Company's common stock at an amount equal to 80% of the average bid price of the Company's common stock on the Over-The-Counter Bulletin Board for a period equal to ten (10) days prior to conversion on the maturity date of September 7, 2007. At any time prior to conversion, the Company will have the right to prepay the promissory notes and accrued but unpaid interest thereon in cash upon 3 days notice, allowing the holders to convert the promissory notes during such notice period. The full principal amount of the Serial Notes is due upon a default under the terms of the Note Agreement. In addition, the Company granted the Investors a security interest in all of its assets (see Note B). The Company agreed to file a registration statement with the SEC to effect the registration of the shares of its common stock underlying the Serial Notes and the warrants within 30 days of the effective date of the Company's pending Registration Statement (SEC File 333 - 122848) being declared effective. The Company also agreed to use its reasonable best efforts to cause the registration statement to be declared effective no later than 180 days after its filing. If the Registration Statement is not filed and declared effective as described above, the Company will be required to pay liquidated damages in the form of cash to the holders of the Serial Notes, in an amount equal to 2% of the unpaid principal balance per month if the above deadlines are not met. In the event of a default on the Serial Notes, the Serial Notes will bear interest at twelve percent (12%) per annum until paid.



The warrants are exercisable for five years from March 8, 2006 until March 7, 2011 at a price of \$0.50 per share. The Company has the right, but not the obligation, to call these warrants for \$1.25 per share at the earlier of (i) one year from issuance or (ii) the date that shares of common stock issuable upon conversion of the Serial Notes and exercise of the warrants are registered for resale and the Company's common stock trades at or above \$1.25 per share for twenty (20) consecutive trading days. The Notes include certain features that are considered embedded derivative financial instruments, such as a variety of conversion options, a variable interest rate feature, events of default and a variable liquidated damages clause.

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**NOTE C - PRIVATE PLACEMENT OF CONVERTIBLE NOTES (continued)**

The initial relative fair value assigned to the embedded derivatives was \$346,500.

In conjunction with the Notes, the Company issued warrants to purchase 3,000,000 shares of common stock. The accounting treatment of the derivatives and warrants requires that the Company record the warrants at their fair values as of the inception date of the debt issuance, which totaled \$512,100.

The Company recorded the fair value of the derivatives (\$346,500) and warrants (\$ 512,100) to debt discount, aggregating \$858,600, which will be amortized to interest expense over the term of the Notes. Amortization of \$143,100 and \$286,200 was recorded for the three and six months ended March 31, 2007, respectively.

The market price of the Company's common stock significantly impacts the extent to which the Company may be required or may be permitted to convert the Serial Notes into shares of the Company's common stock. The lower the market price of the Company's common stock at the due date of September 7, 2007, the more shares the Company will need to issue to convert the principal and interest payments then due on the Notes.

*10% Secured Convertible Promissory Notes dated May 2, 2006*

On May 2, 2006, in connection with a private placement, the Company issued 10% Secured Convertible Promissory Notes in the aggregate principal amount of \$1,000,000 (the "Serial Notes") and warrants to purchase 2,000,000 shares of the Company's common stock to accredited investors. The Serial Notes bear interest at 10%, mature on August 2, 2007 and are convertible into the Company's common stock, at the holder's option, at fifty cents (\$.50) per share during the period from the date of issuance (May 2, 2006) through May 2, 2007. Should the holder of the Serial Note elect not to convert to the Company's common stock on or before May 2, 2007, the outstanding principal, along with accrued and unpaid interest automatically converts to the Company's common stock at an amount equal to 80% of the average bid price of the Company's common stock on the Over-The-Counter Bulletin Board for a period equal to ten (10) days prior to conversion on the maturity date of May 2, 2007. The full principal amount of the Serial Notes is due upon a default under the terms of the Note Agreement. In addition, the Company granted the Investors a security interest in all of its assets (see Note B). The Company agreed to file a registration statement with the SEC to effect the registration of the shares of its common stock underlying the Serial Notes and the warrants within 30 days of the effective date of the Company's pending Registration Statement (SEC File 333 - 122848) being declared effective. The Company also agreed to use its reasonable best efforts to cause the registration statement to be declared effective no later than 180 days after its filing. In the event of a default on the Serial Notes, the Serial Notes will bear interest at twelve percent (12%) per annum until paid.

The warrants are exercisable for four years from May 2, 2007 until May 2, 2011 at a price of \$0.50 per share. The Company has the right, but not the obligation, to call these warrants for \$0.001 per share at the earlier of (i) one year from issuance and (ii) the date that shares of common stock issuable upon conversion of the Serial Notes and exercise of the warrants are registered for resale and the Company's common stock trades at and above \$1.00 per share for twenty (20) consecutive trading days. The Notes include certain features that are considered embedded derivative financial instruments, such as a variety of conversion options, a variable interest rate feature, events of default and a variable liquidated damages clause.

The initial relative fair value assigned to the embedded derivatives was \$82,358.



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**NOTE C - PRIVATE PLACEMENT OF CONVERTIBLE NOTES (continued)**

In conjunction with the Notes, the Company issued warrants to purchase 2,000,000 shares of common stock. The accounting treatment of the derivatives and warrants requires that the Company record the warrants at their fair values as of the inception date of the debt issuance, which totaled \$373,600.

The Company recorded the fair value of the derivatives (\$82,358) and warrants (\$373,600) to debt discount, aggregating \$455,958, which will be amortized to interest expense over the term of the Notes. Amortization of \$174,761 and 265,961 was recorded for the three and six months ended March 31, 2007, respectively.

The market price of the Company's common stock significantly impacts the extent to which the Company may be required or may be permitted to convert the Serial Notes into shares of the Company's common stock. The lower the market price of the Company's common stock at the due date of September 7, 2007, the more shares the Company will need to issue to convert the principal and interest payments then due on the Notes.

*10% Secured Convertible Promissory Notes dated June 15, 2006*

On June 15, 2006, in connection with a private placement, the Company issued 10% Secured Convertible Promissory Notes in the aggregate principal amount of \$2,950,000 (the "Serial Notes") and warrants to purchase 5,900,000 shares of the Company's common stock to accredited investors. The Serial Notes bear interest at 10%, mature on August 2, 2007 and are convertible into the Company's common stock, at the holder's option, at fifty cents (\$.50) per share during the period from the one year from the date of issuance (June 15, 2006) through June 15, 2007. Should the holder of the Serial Note elect not to convert to the Company's common stock on or before June 15, 2007, the outstanding principal, along with accrued and unpaid interest automatically converts to the Company's common stock at an amount equal to 80% of the average bid price of the Company's common stock on the Over-The-Counter Bulletin Board for a period equal to ten (10) days prior to conversion on the maturity date of June 15, 2007. The full principal amount of the Serial Notes is due upon a default under the terms of the Note Agreement. In addition, the Company granted the Investors a security interest in all of its assets (see Note B). The Company agreed to file a registration statement with the SEC to effect the registration of the shares of its common stock underlying the Serial Notes and the warrants within 30 days of the effective date of the Company's pending Registration Statement (SEC File 333 - 122848) being declared effective. The Company also agreed to use its reasonable best efforts to cause the registration statement to be declared effective no later than 180 days after its filing. In the event of a default on the Serial Notes, the Serial Notes will bear interest at twelve percent (12%) per annum until paid.

The warrants are exercisable for four years from June 15, 2007 until June 15, 2011 at a price of \$0.50 per share. The Company has the right, but not the obligation, to call these warrants for \$0.001 per share at the earlier of (i) one year from issuance and (ii) the date that shares of common stock issuable upon conversion of the Serial Notes and exercise of the warrants are registered for resale and the Company's common stock trades at and above \$1.00 per share for twenty (20) consecutive trading days. The Notes include certain features that are considered embedded derivative financial instruments, such as a variety of conversion options, a variable interest rate feature, events of default and a variable liquidated damages clause.

The initial relative fair value assigned to the embedded derivatives was \$175,321.

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**NOTE C - PRIVATE PLACEMENT OF CONVERTIBLE NOTES (continued)**

In conjunction with the Notes, the Company issued warrants to purchase 5,900,000 shares of common stock. The accounting treatment of the derivatives and warrants requires that the Company record the warrants at their fair values as of the inception date of the debt issuance, which totaled \$929,840.

The Company recorded the fair value of the derivatives (\$175,321) and warrants (\$929,840) to debt discount, aggregating \$1,105,161, which will be amortized to interest expense over the term of the Notes. Amortization of \$395,862 and \$616,962 was recorded for the three and six months ended March 31, 2007, respectively.

The market price of the Company's common stock significantly impacts the extent to which the Company may be required or may be permitted to convert the Serial Notes into shares of the Company's common stock. The lower the market price of the Company's common stock at the due date of September 7, 2007, the more shares the Company will need to issue to convert the principal and interest payments then due on the Notes.

*\$1,675,000 Convertible Notes*

Convertible notes payable ("Bridge Unit Offering") in quarterly installments of interest only at 10% per annum, secured by all assets of the Company and due on the earlier of the 9 month anniversary date of the initial closing of the offering or the completion of any equity financing of \$3,000,000 or more; the Company, at its sole discretion may prepay principal at any time without penalty. The Bridge Unit Offering Notes unpaid principal along with accrued and unpaid interest was converted to an aggregate of 4,988,051 shares of the Company's common shares at a price equal to approximately \$0.33 per share during the quarter ended March 31, 2005.

*\$1,465,000 Convertible Notes*

Beginning in December, 2004, the Company sold a 10% convertible debenture in the aggregate amount of \$1,465,000 in a private placement and exempt offerings to sophisticated investors, net of costs and fees.

The Convertible Note's terms called for the debt to automatically convert at \$0.50 per share upon the filing of a registration statement with the Securities and Exchange Commission.

The Company filed the registration statement on February 15, 2005 and the Convertible Notes were converted to an aggregate of 2,930,000 shares of the Company's common stock in February 2005.

As additional consideration for the purchase of the Convertible Notes, the Company granted to the holders warrants entitling it to purchase 2,930,000 common shares of the Company's common stock at the price of \$0.75 per share. These warrants were issued in February, 2005 and lapse if unexercised by February, 2010. A registration rights agreement was executed in December 2004 and consummated in February, 2005 requiring the Company to register the shares of its common stock underlying the Convertible Notes and warrants so as to permit the public resale thereof. The registration rights agreement provided for the payment of liquidated damages of 3.5% of the aggregate Convertible Note financing per month if the stipulated registration deadlines were not met. The liquidated damages, which approximate \$51,275 per month, may be paid, at the Company's option, in cash or unregistered shares of the Company's common stock.



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**NOTE C - PRIVATE PLACEMENT OF CONVERTIBLE NOTES (continued)**

In accordance with Emerging Issues Task Force Issue 98-5, Accounting for Convertible Securities with a Beneficial Conversion Features or Contingently Adjustable Conversion Ratios ("EITF 98-5"), the Company recognized an imbedded beneficial conversion feature present in the Convertible Notes. The Company allocated a portion of the proceeds equal to the intrinsic value of that feature to additional paid-in capital. The Company recognized and measured an aggregate of \$1,465,000 of the proceeds, which is equal to the intrinsic value of the imbedded beneficial conversion feature, to additional paid-in capital and a discount against the Convertible Notes. Since the Convertible Notes were converted to the Company's common stock in February 2005, the debt discount attributed to the beneficial conversion feature of \$1,465,000 was charged to interest expense in its entirety during the six months ended March 31, 2005.

In conjunction with raising capital through the issuance of Convertible Notes, the Company has issued a warrant in February, 2005 that has registration rights for the underlying shares. As the contract must be settled by the delivery of registered shares and the delivery of the registered shares is not controlled by the Company, pursuant to EITF 00-19, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock", the net value of the warrants at the date of issuance was recorded as a warrant liability on the balance sheet at \$3,845,039 and charged to operations as interest expense. Upon the registration statement being declared effective, the fair value of the warrant on that date will be reclassified to equity. The Company initially valued the warrants using the Black-Scholes pricing model with the following assumptions: (1) dividend yield of 0%; (2) expected volatility of 148.66%, (3) risk-free interest rate of 3.21%, and (4) expected life of 3 years.

In connection with the placement of the \$1,465,000 of convertible notes as described above, the Company agreed to registered shares of the Company's common stock underlying certain previously issued and outstanding warrants that were not subject to a registration rights agreement at the time the warrants were issued. These warrants consist of following:

- 105,464 warrants entitling the holder to purchase 105,464 shares of the Company's common stock at the price of \$0.10 per share. These warrants were issued in July, 2004 and lapse if unexercised by July, 2009.
- 1,602,500 warrants entitling the holder to purchase 1,602,500 shares of the Company's common stock at the price of \$0.60 per share. These warrants were issued in October, 2003 and lapse if unexercised by October, 2008.

As a result, the Company is required to classify the warrants as derivative liabilities and mark them to market at each reporting date. The fair value of the warrants that were subject to registration reclassified as liabilities from additional paid in capital at February 2005 totaled \$3,108,851. Upon the registration statement being declared effective, the fair value of the warrants on that date will be reclassified to equity. The Company initially valued the warrants using the Black-Scholes pricing model with the following assumptions: (1) dividend yield of 0%; (2) expected volatility of 148.66%, (3) risk-free interest rate of 3.21%, and (4) expected life of 3 years.

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**NOTE C - PRIVATE PLACEMENT OF CONVERTIBLE NOTES (continued)**

*\$7,371,000 Convertible Notes*

In January and February, 2005, the Company sold a 10% convertible debenture in the aggregate amount of \$7,371,000 in a private placement and exempt offerings to sophisticated investors, net of costs and fees.

The Convertible Note's terms called for the debt to automatically convert at \$0.50 per share upon the filing of a registration statement with the Securities and Exchange Commission.

The Company filed the registration statement on February 15, 2005 and the Convertible Notes were converted to an aggregate of 14,742,000 shares of the Company's common stock.

As additional consideration for the purchase of the Convertible Notes, the Company granted to the holders warrants entitling it to purchase 14,742,000 common shares of the Company's common stock at the price of \$0.75 per share.

These warrants lapse if unexercised by February, 2010. A registration rights agreement was executed and consummated in January, 2005 requiring the Company to register the shares of its common stock underlying the Convertible Notes and warrants so as to permit the public resale thereof. The registration rights agreement provided for the payment of liquidated damages of 3.5% of the aggregate Convertible Note financing per month if the stipulated registration deadlines were not met. The liquidated damages, which approximate \$257,985 per month, may be paid, at the Company's option, in cash or unregistered shares of the Company's common stock.

In accordance with Emerging Issues Task Force Issue 98-5, Accounting for Convertible Securities with a Beneficial Conversion Features or Contingently Adjustable Conversion Ratios ("EITF 98-5"), the Company recognized an imbedded beneficial conversion feature present in the Convertible Notes. The Company allocated a portion of the proceeds equal to the intrinsic value of that feature to additional paid-in capital. The Company recognized and measured an aggregate of \$7,731,000 of the proceeds, which is equal to the intrinsic value of the imbedded beneficial conversion feature, to additional paid-in capital and a discount against the Convertible Notes. Since the Convertible Notes were converted to the Company's common stock in February, 2005, the debt discount attributed to the beneficial conversion feature of \$7,371,000 was charged to interest expense in its entirety during the six months ended March 31, 2005.

In conjunction with raising capital through the issuance of Convertible Notes, the Company has issued warrants that have registration rights for the underlying shares. As the contract must be settled by the delivery of registered shares and the delivery of the registered shares is not controlled by the Company, pursuant to EITF 00-19, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock", the net value of the warrants at the date of issuance was recorded as a warrant liability on the balance sheet \$19,303,175 and charged to operations as interest expense. Upon the registration statement being declared effective, the fair value of the warrant on that date will be reclassified to equity. The Company initially valued the warrants using the Black-Scholes pricing model with the following assumptions: (1) dividend yield of 0%; (2) expected volatility of 152.59%, (3) risk-free interest rate of 3.67%, and (4) expected life of 5 years.



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**NOTE D - CAPITAL STOCK**

The Company is authorized to issue 10,000,000 shares of preferred stock with a \$0.001 par value per share. On May 17, 2007 the Company amended its Articles of Incorporation to increase the number of authorized shares of common stock of the Company, \$0.001 par value per share, to 410,000,000 shares following stockholder approval at the annual meeting of stockholders held on May 16, 2007. The Company had previously amended its Articles of Incorporation on March 3, 2005 to increase the number of authorized shares of common stock of the Company, \$0.001 par value per share, to 250,000,000 shares, following the approval by written consent of shareholders holding a majority of the outstanding common stock. In February 2005, the Company passed a resolution authorizing change in the par value per common shares from \$0.50 per share to \$0.001 per share.

During the period September 16, 2002 through September 30, 2003, the Company issued 100,000 shares of common stock in exchange for reimbursement of services provided by the founders of the Company. The Company valued the shares issued at approximately \$1,000, which represents the fair value of the services received which did not differ materially from the value of the stock issued.

In October, 2002, the Company issued 10,178,352 shares of common stock in exchange for the previously issued 100,000 shares to the Company's founders in connection with the merger with Prohealth Medical Technologies, Inc.

In October, 2002 the Company canceled 100,000 shares of common stock issued to the Company's founders.

During the fiscal year ended September 30, 2003, the Company issued 2,369,130 shares of common stock, net of cancellation of 860,000 shares in exchange for consulting services. The Company valued the shares issued at \$2,191,227, net of cancellation of \$60,008, which represents the fair value of the services received which did not differ materially from the value of the stock issued.

In November 2003, the Company issued 876,000 shares of common stock in exchange for subscription at approximately \$0.065 per share.

In January 2003, the Company issued 1,500,000 shares of common stock in exchange for a licensing agreement. The Company valued the shares issued at approximately \$0.065 per share, which represents the fair value of the license received which did not differ materially from the value of the stock issued. The Company charged the cost of the license to operations.

In March 2003, the Company issued 10,140,000 shares of common stock to Company's founders in exchange for services. In accordance with EITF 96-18 the measurement date to determine fair value was in September 2002. This was the date at which a commitment for performance by the counter party to earn the equity instrument was reached. The Company valued the shares issued at approximately \$0.0001 per share, which presents the fair value of the services received which did not differ materially from the value of the stock issued.

In connection with the Company's acquisition of ProHealth, the controlling owner of ProHealth granted the Company an option to acquire up to 8,500,000 shares of the Company's common stock in exchange for \$100,000. The option expired on December 10, 2004. On June 30, 2003, the Company exercised its option and acquired 7,500,000 common shares under this agreement in exchange for an \$88,500 convertible promissory note payable to the former controlling owner. The Company had an option through December 10, 2004 to acquire the remaining 1,000,000 shares from the

former controlling owner in exchange for \$11,500. On June 30, 2003, the Company retired the 7,500,000 shares common acquired pursuant to the option agreement.

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**NOTE D - CAPITAL STOCK (continued)**

In September 2003, the Company issued 19,200 shares of common stock for cash previously subscribed at \$2.50 per share.

During the fiscal year ended September 30, 2003, the Company issued 154,000 shares of common stock in exchange for previously issued options to purchase the Company's common stock at \$1.00 per share.

During the fiscal year ended September 30, 2003, the Company issued 74,400 shares of common stock in exchange for cash at approximately \$0.89 per share.

In October 2003, the Company issued 15,000 shares of convertible preferred stock in exchange for services. The Company valued the shares issued at the \$15 par value and recorded the value for services when the shares were converted into common shares as identified below.

During the fiscal year ended September 30, 2004, the Company issued 5,149,472 shares of common stock, net of cancellation of 155,000 shares, in exchange for consulting services. The Company valued the shares issued at \$8,787,315, net of cancellation of \$408,575, which represents the fair value of the services received which did not differ materially from the value of the stock issued.

During the fiscal year ended September 30, 2004, the Company issued 340,500 shares of common stock for shares previously subscribed at approximately \$2.04 per share.

In March 2004, the Company issued 55,000 of common stock for options exercised at \$1.00 per share.

During the fiscal year ended September 30, 2004, the Company converted 15,000 preferred shares into 375,000 shares of common stock at \$1.47 per share in exchange for employee services valued at \$549,750.

In June 2004, the Company sold 250,000 shares of common stock at \$1.00 per share for total proceeds of \$250,000 pursuant to a private placement.

In September 2004, the Company issued 60,000 convertible preferred shares at \$25, in exchange for consulting services valued at \$1,500,000.

During the fiscal year ended September 30, 2005, the Company issued 11,040,647 shares of common stock, net of cancellation of 2,329,600 shares, in exchange for consulting and employee services. The Company valued the shares issued at \$13,008,371, net of cancellation of \$1,328,269, which represents the fair value of the services received which did not differ materially from the value of the stock issued.

During the fiscal year ended September 30, 2005, the Company issued 1,500,000 shares of common stock for shares previously subscribed at approximately \$0.54 per share.

During the fiscal year ended September 30, 2005, the Company issued 267,500 shares of common stock for warrants and options exercised at approximately \$0.39 per share.

In October 2004, the Company issued 500,000 shares of common stock in exchange for debt at \$0.50 per share.

In December 2004, the Company issued net 5,500,000 shares of common stock for default as per terms of notes payable for \$88,500. Out of total, 3,500,000 shares were retained in escrow on behalf of another party for future deferred compensation.

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**NOTE D - CAPITAL STOCK (continued)**

In February 2005, the Company in exchange for a related party note in the outstanding principal amount of \$600,000 and as settlement for certain claims related thereto issued 1,500,000 shares of common stock using a price of \$1.31 per share. (See note G)

In March, 2005, the Company granted an aggregate of 300,000 stock options to employees that vested immediately. The exercise prices of the stock options granted were below the fair value of the Company's common stock at the grant date. Compensation expense of \$180,000 and \$0 was charged to operations during the period ended March 31, 2005 and 2004, respectively.

In June 2005, the Company cancelled 300,000 stock options previously granted valued at \$180,000. In accordance with EITF 96-18 the measurement date to determine fair value was the date at which a commitment for performance by the counter party to earn the equity instrument was reached. The Company valued the shares issued for consulting services at the rate which represents the fair value of the services received which did not differ materially from the value of the stock issued.

In July 2005, the Company issued 36 million shares in exchange for intellectual property at approximately \$0.67 per share for a total of \$24,120,000. The value of the acquired intangible assets was established at \$9,430,900, with the balance of the purchase price, or \$14,689,100, charged to operations as a cost of the transaction. (See Note B)

In 2005, the Company issued 8,550,000 shares of its common stock without restriction to employees in exchange for services rendered. The Company valued the shares issued at market value and charged to operations in the period the shares were issued. The Company investigated the circumstances surrounding the issuance of the shares and the possible subsequent resale of certain of the shares on the open market and the possibility of violations of securities laws and reported its findings to the Securities and Exchange Commission (see Note H).

Until the Company successfully completes its pending registration statement on SEC Form SB-2, the Company is subject to liquidated damages (see Note D). In connection with the \$1,465,000 and \$7,371,000 million convertible debt financing, the Company was obligated to deliver registered shares underlying the convertible notes and warrants by July 2005. Since the registration was not effective by July 2005, the Company has been accruing and charging to operations the stipulated liquidated damages in shares of the Company's common stock accruing at a rate of 3.5% per month on the face value of the previously issued convertible notes. During the year ended September 30, 2005, the Company has paid and charged to operations penalties of \$776,529 in the form of 605,382 unregistered shares of its common stock to the former note holders.

In October, 2005, the Company issued 400,000 shares of common stock subscribed for cash at \$0.50 per share for a total of \$200,000 pursuant to the terms of a subscription payable. This issuance is considered exempt under Regulation D of the Securities Act of 1933 and Rule 506 promulgated thereunder.

In October 2005, the Company issued 100,000 shares of common stock in exchange for consulting services. The Company valued the shares issued at approximately \$0.75 per share for a total of \$75,000, which represents the fair value of the services received which did not differ materially from the value of the stock issued.

In October 2005, the Company cancelled 350,000 shares previously issued for services valued at \$210,000.



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**NOTE D - CAPITAL STOCK (continued)**

In December, 2005, the Company issued 40,000 shares of common stock subscribed for cash at \$0.50 per share for a total of \$20,000 pursuant to the terms of a subscription payable. This issuance is considered exempt under Regulation D of the Securities Act of 1933 and Rule 506 promulgated thereunder.

For the fiscal year ended September 30, 2005, the Company issued a total of 2,096,139 penalty shares pursuant to a registration rights agreement. In connection with the 7,371,000 million convertible debt financing in the quarter ended March 31, 2005, the Company was obligated to complete a stock registration by July 2005. Since the registration statement was not effective by July 2005, the Company paid the required \$773,959 of liquidated damages in shares of Company stock accruing at the rate of 3.5% per month on the face value of the Notes for the month of September 2005. The Company valued the shares issued at approximately \$0.30 per share for a total of \$773,959. The Company continues to accrue the penalties relating to the pending registration statement.

In January, 2006, the Company cancelled 250,000 shares previously issued for services valued at \$150,000.

In January 2006, the Company issued 2,096,139 penalty shares pursuant to a registration rights agreement. In connection with the 7,371,000 million convertible debt financing in the quarter ended March 31, 2005, the Company was obligated to complete a stock registration by July 2005. Since the registration statement was not effective by July 2005, the Company paid the required \$257,985 of liquidated damages in shares of Company stock accruing at the rate of 3.5% per month on the face value of the Notes for the month of November and December 2005. The Company valued the shares issued at approximately \$0.25 per share for a total of \$515,973. The Company continues to accrue the penalties relating to the pending registration statement.

In February 2006, the Company issued 160,000 shares of common stock in exchange for consulting services. The Company valued the shares issued at approximately \$0.17 per share for a total of \$27,200, which represents the fair value of the services received which did not differ materially from the value of the stock issued

In February 2006, the Company issued 3,800,000 shares of common stock in exchange for consulting services. The Company valued the shares issued at approximately \$0.16 per share for a total of \$608,000, which represents the fair value of the services received which did not differ materially from the value of the stock issued

In March 2006, the Company cancelled 150,000 shares previously issued for services valued at \$120,000.

In December 2006, the Company issued 180,000 shares of common stock in settlement of a previously incurred related party debt of \$410,429. The Company valued the shares issued at approximately \$0.09 per share for a total of \$16,200, which represents the fair value of the shares at the date of issuance. The Company recorded the balance of the debt, or \$394,229 from the extinguishment of a related party debt as additional paid in capital.

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**NOTE E - STOCK OPTIONS AND WARRANTS***Warrants*

The following table summarizes the changes in warrants outstanding and the related prices for the shares of the Company's common stock issued to non-employees of the Company. These warrants were granted in lieu of cash compensation for services performed or financing expenses in connection with the sale of the Company's common stock.

Exercise Prices	Number Outstanding	Warrants	Weighted	Weighted	Exercisable
		Outstanding Remaining Contractual Life (Years)	Average Exercise Price	Average Exercise Price	Weighted Average Exercise Price
\$0.09	18,900,000	4.42	\$0.09	18,900,000	\$0.09
\$0.10	105,464	2.29	\$0.10	105,464	\$0.10
\$0.20	5,000	1.64	\$0.20	5,000	\$0.20
\$0.50	16,450,000	3.90	\$0.50	16,450,000	\$0.50
\$0.55	9,000,000	1.22	\$0.55	9,000,000	\$0.55
\$0.60	8,847,000	2.17	\$0.60	8,847,000	\$0.60
\$0.70	950,000	0.64	\$0.70	950,000	\$0.70
\$0.75	17,727,000	2.50	\$0.75	17,727,000	\$0.75
	71,984,464			71,984,464	

Transactions involving warrants are summarized as follows:

	Number of Shares	Weighted Average Price Per Share
Balance, September 30, 2004	4,870,253	\$ 0.63
Granted	32,873,000	0.71
Exercised	(142,500)	.034
Canceled or expired	(731,289)	0.65
Balance, September 30, 2005	36,869,464	0.67
Granted	35,500,000	0.29
Exercised	-	-
Canceled or expired	-	-
Outstanding at September 30, 2006	72,369,464	0.48
Granted	-	-
Exercised	-	-
Canceled or expired	(385,000)	(0.71)
Balance, March 31, 2007	71,984,464	\$ 0.48





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**NOTE E - STOCK OPTIONS AND WARRANTS (continued)**Employee Stock Options

The following table summarizes the changes in options outstanding and the related prices for the shares of the Company's common stock issued to employees of the Company under a non-qualified employee stock option plan.

Options Outstanding			Options Exercisable		
Exercise Prices	Number Outstanding	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price
\$ 0.68	3,660,000	2.50	\$ 0.68	3,660,000	\$ 0.68
0.09	2,000,000	4.42	0.09	2,000,000	0.09
	5,660,000			5,660,000	0.47

Transactions involving stock options issued to employees are summarized as follows:

	Number of Shares	Weighted Average Exercise Price Per Share
Outstanding at October 1, 2005	3,660,000	\$ 0.68
Granted	2,000,000	0.09
Exercised	-	-
Cancelled or expired	-	-
Outstanding at September 30, 2006	5,660,000	\$ 0.47
Granted	-	-
Exercised	-	-
Canceled or expired	-	-
Outstanding at December 31, 2006	5,660,000	\$ 0.47

The Company did not grant any employee options during the six months ended March 31, 2007.

Effective January, 2006, the Company adopted SFAS 123R and recognized compensation expense in its financial statements in fiscal 2006. Prior to the adoption of SFAS 123R, the Company accounted for its stock option plans according to Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees." Accordingly, no compensation costs were recognized upon issuance or exercise of stock options for fiscal 2005.

SFAS No. 123, "Accounting for Stock-Based Compensation," required the disclosure of the estimated fair value of employee option grants and their impact on net income using option pricing models that are designed to estimate the value of options that, unlike employee stock options, can be traded at any time and are transferable. In addition to restrictions on trading, employee stock options may include other restrictions such as vesting periods. Further, such models require the input of highly subjective assumptions, including the expected volatility of the stock price.

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**NOTE F - DEBT DERIVATIVE AND WARRANT LIABILITY**

In accordance with SFAS 133 "Accounting for Derivative Instruments and Hedging Activities and EITF 00-19 "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock", the Company accounted for identified embedded derivatives and warrants to purchase its common stock that provide for the payment of liquidated damages if the stipulated registration deadlines were not met as liabilities.

As of the date of this filing, the registration statement has not yet been declared effective by the SEC. The Company determined the fair value of the embedded derivatives and valued the warrants using the Black-Scholes option pricing model. Assumptions regarding the life were one to five years, expected dividend yield of 0%, a risk free rate of 4.54 to 5.04%, and a volatility of 100.22%. The determined value of both the warrants and the underlying embedded derivatives as of March 31, 2007 was \$8,820,085. The net change in the fair value of the derivative and warrant liability values from September 30, 2006 has been recorded as a gain from change in debt derivative and warrant liabilities in the consolidated condensed statement of operations.

**NOTE G- RELATED PARTY TRANSACTIONS**

On December 12, 2006, the Company issued 180,000 shares of its common stock as settlement of the outstanding related party note payable of \$410,429 and related accrued interest of \$8,884

The Company's officers have advanced funds to the Company for travel related and working capital purposes. No formal repayment terms or arrangements exist. There were no advances due at March 31, 2007.

On July 12, 2005, the Company entered into a consulting agreement with Timpix International Limited ("Timpix") for the consulting services of three former Biowell employees, Drs. Jun-Jei Sheu, Ben Liang and Johnson Chen. The consulting agreement is for the shorter of two years, or until all of the consultants have obtained a visa to work in the United States and execute employment agreements with the Company. The consulting agreement shall automatically renew for one year periods until terminated. Pursuant to the consulting agreement, the Company is obligated to pay \$47,000 per month, which is apportioned at \$20,000 per month for Mr. Sheu, \$15,000 per month for Mr. Liang and \$12,000 per month for Mr. Chen. In the event that either of Messrs. Sheu, Liang or Chen becomes employed by us, the monthly consulting fee shall be reduced accordingly.

On November 13, 2006, the Company restructured its consulting agreement with Timpix International Limited ("Timpix") for consulting services of three former Biowell employees. Drs Jun-Jei Sheu, Ben Liang and Johnson Chen. The restructured consulting agreement expires on July 11, 2007 or when all of the consultants have obtained a visa to work in the United States and execute employment agreements with the Company, whichever comes first. The revised consulting agreement shall automatically renew for one year periods until terminated. Pursuant to the agreement, the Company is obligated to pay \$120,000, \$100,000 and \$80,000 per year pro-rated for each week, or part thereof, of time spent within the United States providing full time services for Drs Jun-Jei Sheu, Ben Lang and Johnson Chen, respectively. The Company is obligated to provide a corporate house available for the Consultants while working in the United States. All previous fees incurred through November 13, 2006 have been waived.

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**NOTE G- RELATED PARTY TRANSACTIONS (continued)**

In July 2005, the Company entered into a license agreement with Biowell, whereby the Company granted Biowell an exclusive license to sell, market, and sub-license the Company's products in selected Asian countries. The exclusive license for such selected territories is for an initial period from July 2005 through December 31, 2010, and if Biowell meets its performance goals, the license agreement will extend for an additional five year term. The license agreement gives Biowell the initial rights to future anti-fraud biotechnologies developed by the Company and also new applications for the existing technology that may be developed for the marketplace as long as the license agreement remains in effect. In the event that Biowell shall sub-license the products within its territories, Biowell shall pay the Company 50% of all fees, payments or consideration or any kind received in connection with the grant of the sublicense. Biowell is required to pay a royalty of 10% on all net sales made and is required to meet certain minimum annual net sales in its various territories. Cumulative royalties earned from the period July 2005 through March 31, 2007 totaled \$34,698. Net amounts owed to the Company by Biowell in connection with the royalty agreement as of March 31, 2007 were \$-0-.

**NOTE H - COMMITMENTS AND CONTINGENCIES**

*Operating Lease Commitments*

The Company leases office space under an operating lease in Stony Brook, New York for its corporate use from an entity controlled by significant former shareholder, expiring in November 2007. In November 2005, the Company vacated the Los Angeles facility to relocate to the new Stony Brook, New York address. Total lease rental expenses for the six months ended March 31, 2007 was \$25,000.

*Employment and Consulting Agreements*

The Company has consulting agreements with outside contractors, certain of whom are also Company stockholders. The Agreements are generally month to month.

On July, 12, 2005, the Company entered into a consulting agreement with Timpix for the consulting services of three former Biowell employees, Drs. Jun-Jei Sheu, Ben Liang and Johnson Chen. On November 13, 2006, the Company restructured its consulting agreement with Timpix International Limited ("Timpix") for consulting services of three former Biowell employees. Drs Jun-Jei Sheu, Ben Liang and Johnson Chen. The restructured consulting agreement expires on July 11, 2007 or when all of the consultants have obtained a visa to work in the United States and execute employment agreements with the Company, whichever comes first. (see Note G above)

*Litigation*

The Company is subject to other legal proceedings and claims, which arise in the ordinary course of its business.

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**NOTE H - COMMITMENTS AND CONTINGENCIES (continued)**

*Paul Reep v. Applied DNA Sciences, Inc., Case No.: BC345702*

Plaintiff Paul Reep, a former employee, commenced this action against the Company on January 10, 2006. Mr. Reep asserted eight causes of action for breach of contract, breach of an oral agreement, negligent misrepresentation, interference with prospective business advantages, defamation, fraud, accounting and constructive trust, unjust enrichment. The relief sought included declaratory relief, unspecified compensatory damages, unpaid salary, unspecified penalties under the California Labor Code, interest, and attorneys' fees. We successfully moved the court to indefinitely stay all proceedings in this matter in light of a forum selection clause designating Nevada state courts as the proper forum. On April 11, 2007, Paul Reep filed suit against the Company, Applied DNA Operations Management, Inc., APDN (B.V.I.), Inc., Jun-Jei Sheu, Ben Liang, James A. Hayward, Larry Lee and Peter Brocklesby in the Clark County District Court, Nevada (Paul Reep v. Applied DNA Sciences, et al., Clark County District Court Case No. A539250). The action is a refiling of a prior lawsuit (Paul Reep v. Applied DNA Sciences, Inc., U.S. District Court, Central District of California, Case No.: BC345702). The complaint alleges causes of action for breach of written contract, breach of oral contract, defamation, fraud and violations of the California Labor Code, and seeks approximately \$360,000 in specified damages, additional damages according to proof, potential punitive damages, and fees and costs. The Company has not been served with the complaint or summons with respect to this matter. The Company disputes all of the allegations and intends to vigorously defend this action. This matter is in its early stages.

*Douglas A. Falkner v. Applied DNA Sciences, Inc./N.C. Industrial Commission File No. 585698*

Plaintiff Douglas Falkner ("Falkner") filed a worker's compensation claim in North Carolina for an alleged work-related neck injury that he alleges occurred on January 14, 2004. Falkner worked as Business Development and Operations Manager at our sole East Coast office at the time of the alleged injury. Plaintiff Falkner was the only employee employed by the Company in North Carolina at the time of the alleged injury and we have employed no other employees in North Carolina at any other time. The claim has been denied and is being defended on several grounds, including the lack of both personal and subject matter jurisdiction. Specifically, the Company contends that it did not employ the requisite minimum number of employees in North Carolina at the time of the alleged injury and that the company is therefore not subject to the North Carolina Workers' Compensation Act. The claim was originally set for hearing in January 2007, but was continued to allow the parties to engage in further discovery.

*Settlement of Litigation*

In May 2007, the Company settled certain pending litigation and other claims arising out of certain former employees' and consultants' prior employment and consulting relationships with the Company (see Note J).

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**NOTE H - COMMITMENTS AND CONTINGENCIES (continued)**

*Registration of Company's Shares of Common Stock*

Until the Company successfully completes its pending registration statement on SEC Form SB-2, the Company is subject to liquidated damages (see Notes D and H). In connection with the \$1,465,000 and \$7,371,000 million convertible debt financing during the quarters ended December 31, 2004 and March 31, 2005, respectively, the Company was obligated to deliver registered shares underlying the convertible notes and warrants by July 2005 (see Note C). Since the registration was not effective by July 2005, the Company has been accruing and charging to operations the stipulated liquidated damages in shares of Company stock accruing at the rate of 3.5% per month on the face value of the previously issued convertible notes. During the year ended September 30, 2006, the Company has paid and charged to operations penalties of \$773,958 in the form of unregistered shares of its common stock to the former note holders, and has accrued and charged to operations an additional \$6,232,666 representing unpaid penalties through March 31, 2007.

*Matters Voluntarily Reported to the SEC and Securities Act Violations*

We previously disclosed that we investigated the circumstances surrounding certain issuances of 8,550,000 shares to employees and consultants in July 2005 (see Note G), and had engaged our then new outside counsel to conduct this investigation. We have voluntarily reported our current findings from the investigation to the SEC, and we have agreed to provide the SEC with further information arising from the investigation. We believe that the issuance of 8,000,000 shares to employees in July 2005 was effectuated by both our former President and our former Chief Financial Officer/Chief Operating Officer without approval of the Board of Directors. These former officers received a total of 3,000,000 of these shares. In addition, it appears that the 8,000,000 shares issued in July 2005, as well as an additional 550,000 shares issued to employees and consultants in March, May and August 2005, were improperly issued without a restrictive legend stating that the shares could not be resold legally except in compliance with the Securities Act of 1933, as amended. The members of our management who effectuated the stock issuances that are being examined in the investigation no longer work for us. In the event that any of the exemptions from registration with respect to the issuance of the Company's common stock under federal and applicable state securities laws were not available, the Company may be subject to claims by federal and state regulators for any such violations. In addition, if any purchaser of the Company's common stock were to prevail in a suit resulting from a violation of federal or applicable state securities laws, the Company could be liable to return the amount paid for such securities with interest thereon, less the amount of any income received thereon, upon tender of such securities, or for damages if the purchaser no longer owns the securities. As of the date of these financial statements, the Company is not aware of any alleged specific violation or the likelihood of any claim. There can be no assurance that litigation asserting such claims will not be initiated, or that the Company would prevail in any such litigation.

The Company is unable to predict the extent of its ultimate liability with respect to any and all future securities matters. The costs and other effects of any future litigation, government investigations, legal and administrative cases and proceedings, settlements, judgments and investigations, claims and changes in this matter could have a material adverse effect on the Company's financial condition and operating results

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**NOTE I - RESTATEMENT OF QUARTERLY FINANCIAL STATEMENTS**

The accompanying condensed consolidated financial statements as of March 31, 2006 and the three and six months ended March 31, 2006 have been restated to correct the following errors in its previously issued financial statements.

- In connection with our review of our outstanding warrants and options to acquire our Company's stock, the Company determined \$329,700 and \$659,400 (three and six months ended March 31, 2006, respectively) of liquidated damages payable to investors pursuant to the terms of the Registration Rights Agreement had not been accounted for and recorded as a selling, general and administrative expense.
- The Company capitalized financing costs previously charged to selling, general and administrative for the three months ended March 31, 2006.
- In connection with our review of our outstanding warrants and options to acquire our Company's stock, the Company determined the issuance of 5,500,000 warrants to acquire the Company's common stock in connection with the issuance of debt was erroneously valued at \$563,750 and was erroneously charged to selling, general and administrative expense; the fair value of the warrants was \$1,758,900 and has been charged to interest expense.
- In conjunction with raising capital through the issuance of Convertible Notes, the Company has issued warrants that have registration rights for the underlying shares. As the contract must be settled by the delivery of registered shares and the delivery of the registered shares is not controlled by the Company, pursuant to EITF 00-19, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock", the net value of the warrants at the date of issuance was recorded as a warrant liability on the balance sheet \$512,100 and charged to operations as interest expense. Upon the registration statement being declared effective, the fair value of the warrant on that date will be reclassified to equity. The Company initially valued the warrants using the Black-Scholes pricing model with the following assumptions: (1) dividend yield of 0%; (2) expected volatility of 154.43%, (3) risk-free interest rate of 4.75%, and (4) expected life of 5 years.

The impact of these restatement adjustments is to decrease the reported net income by \$1,303,202 from \$3,363,553 to \$2,033,351 for the three months ended March 31, 2006 and to decrease the reported net income by \$4,193,955 from \$9,039,717 to \$4,845,762 for the six months ended March 31, 2006. There was no effect on total cash flows provided by (used in) operations, investing or financing activities.

The following are reconciliations of the Company's condensed consolidated statements of income for the three months ended March 31, 2006:

**1. Under Selling, general and administrative:**

- (a) Recording three month liquidation damages relating to December 2004 Convertible note discussed in Note C above of \$153,825.
- (b) Recording three month liquidation damages relating to 2003 bridge Convertible note discussed in Note C above of \$175,875.



(c) Capitalize \$390,000 finance costs incurred in conjunction with financing.

Net effect: \$60,300 decrease in Selling, general and administrative expense.

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**APPLIED DNA SCIENCES, INC**  
**(a development stage company)**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**MARCH 31, 2007**  
**(Unaudited)**

**NOTE I - RESTATEMENT OF QUARTERLY FINANCIAL STATEMENTS (continued)**

**2.** Under Net gain/loss on reevaluation of debt derivative and warrant liability:

(a) Correct the adjustment in fair value of warrant liability from previous filing by a reduction of \$878,403.

**3.** Under Interest Income (expense):

(a) In conjunction with raising capital through the issuance of Convertible Notes, the Company has issued warrants that have registration rights for the underlying shares. As the contract must be settled by the delivery of registered shares and the delivery of the registered shares is not controlled by the Company, pursuant to EITF 00-19, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock", the net value of the warrants at the date of issuance was recorded as a warrant liability on the balance sheet \$512,100 and charged to operations as interest expense. Upon the registration statement being declared effective, the fair value of the warrant on that date will be reclassified to equity. The Company initially valued the warrants using the Black-Scholes pricing model with the following assumptions: (1) dividend yield of 0%; (2) expected volatility of 154.43%, (3) risk-free interest rate of 4.75%, and (4) expected life of 5 years.

The following are reconciliations of the Company's condensed consolidated statements of income for the six months ended March 31, 2006:

**4.** Under Selling, general and administrative:

(a) Recording six month liquidation damages relating to December 2004 Convertible note discussed in Note C above of \$307,650.

(b) Recording three month liquidation damages relating to 2003 bridge Convertible note discussed in Note C above of \$351,750.

(c) Capitalize \$390,000 finance costs incurred in conjunction with financing.

(d) In connection with our review of our outstanding warrants and options to acquire our Company's stock, the Company determined the issuance of 5,500,000 warrants to acquire the Company's common stock in connection with the issuance of debt was erroneously valued at \$563,750 and was erroneously charged to selling, general and administrative expense; the fair value of the warrants was \$ 1,758,900 and has been charged to interest expense.

The net effect to selling, general and administrative is a reduction of \$294,250, net of items a, b, c and d above.

**5.** Under Net gain/loss on reevaluation of debt derivative and warrant liability:

(a) Correct the adjustment in fair value of warrant liability from previous filing by a reduction of \$2,217,306.

**APPLIED DNA SCIENCES, INC**  
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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**MARCH 31, 2007**  
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**NOTE I - RESTATEMENT OF QUARTERLY FINANCIAL STATEMENTS (continued)**

**6. Under Interest Income (expense):**

- (a) In conjunction with raising capital through the issuance of Convertible Notes, the Company has issued warrants that have registration rights for the underlying shares. As the contract must be settled by the delivery of registered shares and the delivery of the registered shares is not controlled by the Company, pursuant to EITF 00-19, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock", the net value of the warrants at the date of issuance was recorded as a warrant liability on the balance sheet \$1,758,900 and charged to operations as interest expense. Upon the registration statement being declared effective, the fair value of the warrant on that date will be reclassified to equity. The Company initially valued the warrants using the Black-Scholes pricing model with the following assumptions: (1) dividend yield of 0%; (2) expected volatility of 156%, (3) risk-free interest rate of 4.55%, and (4) expected life of 5 years.
- (b) In conjunction with raising capital through the issuance of Convertible Notes, the Company has issued warrants that have registration rights for the underlying shares. As the contract must be settled by the delivery of registered shares and the delivery of the registered shares is not controlled by the Company, pursuant to EITF 00-19, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock", the net value of the warrants at the date of issuance was recorded as a warrant liability on the balance sheet \$512,100 and charged to operations as interest expense. Upon the registration statement being declared effective, the fair value of the warrant on that date will be reclassified to equity. The Company initially valued the warrants using the Black-Scholes pricing model with the following assumptions: (1) dividend yield of 0%; (2) expected volatility of 154.43%, (3) risk-free interest rate of 4.75%, and (4) expected life of 5 years.

The net effect to Interest expense is an increase of \$2,271,000, net of items a and b above. (\$1 rounding.)

**APPLIED DNA SCIENCES, INC**  
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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**MARCH 31, 2007**  
**(Unaudited)**

**NOTE I - RESTATEMENT OF QUARTERLY FINANCIAL STATEMENTS (continued)**

Condensed Consolidated Statement of Income (Losses)  
For the Three Months Ended March 31, 2006

	<b>As previously</b>				<b>As Restated</b>
	<b>Reported</b>	<b>Adjustment</b>	<b>Reference</b>		
Selling, general & administrative	\$ 1,009,934	\$ (60,300)	1	\$	949,634
Research and development	\$ 75,033	\$			75,033
Depreciation	\$ 341,676	\$		\$	341,676
Total operating expenses	\$ 1,426,643	\$ (60,300)	1	\$	1,366,343
Net loss from operations	\$ (1,426,643)	\$ (60,300)	1	\$	(1,366,343)
Net gain (loss) in fair value of debt derivative and warrant liability	\$ 4,846,273	\$ 878,403	2	\$	3,967,870
Other income (expense)	\$ 3,520	\$		\$	3,520
Interest income (expense)	\$ (59,597)	\$ (512,099)	3	\$	(571,696)
Net income	\$ 3,363,553	\$ (1,330,202)	1,2,3	\$	2,033,351
Net income per share-basic	\$ 0.03	(0.01)		\$	0.02
Net income (loss) per share-fully diluted	0.03	(0.05)		\$	(0.02)

Condensed Consolidated Statement of Income (Losses)  
For the Six Months Ended March 31, 2006

Selling, general & administrative	\$ 3,088,661	\$ (294,350)	4	\$	2,794,311
Research and development	\$ 91,303	\$			91,303
Depreciation	\$ 684,375	\$		\$	684,375
Total operating expenses	\$ 3,864,339	\$ (294,350)	4	\$	3,569,989
Net loss from operations	\$ (3,864,339)	\$ (294,350)	4	\$	(3,569,989)
Net gain (loss) in fair value of debt derivative and warrant liability	\$ 12,973,966	\$ 2,217,306	5	\$	10,756,660
Other income (expense)	\$ 9,493	\$		\$	9,493
Interest income (expense)	\$ (79,403)	\$ (2,270,999)	6	\$	(2,350,402)
Net income	\$ 9,039,717	\$ (4,193,955)	4,5,6	\$	4,845,762
Net income per share-basic	\$ 0.08	(0.04)		\$	0.04
Net income (loss) per share-fully diluted	0.08	(0.11)		\$	(0.03)

**APPLIED DNA SCIENCES, INC**  
**(a development stage company)**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**MARCH 31, 2007**  
**(Unaudited)**

**NOTE I - RESTATEMENT OF QUARTERLY FINANCIAL STATEMENTS (continued)**

Condensed Consolidated Statement of Cash Flows  
For the Six Months Ended March 31, 2006

Cash flows from operating activities				
Net income (loss)	\$ 9,039,717	\$ (4,193,955)	4,5,6	\$ 4,845,762
Adjustments to reconcile to net used in operating activities				
Depreciation and amortization	\$ 684,375	\$		\$ 684,375
Warrants issued to consultants	\$ 43,100	\$		\$ 43,100
Income attributable to repricing of warrants and debt derivatives	\$ (12,973,966)	\$ 2,217,306	5	\$ (10,756,660)
Financing costs attributable to issuance of warrants	\$ -	\$ 2,271,000	6	\$ 2,271,000
Amortization of debt discount attributable to convertible debentures	\$ 35,390	\$		\$ 35,390
Common stock issued in exchange for services	\$ 1,273,950	\$ (563,750)	4d	\$ 710,200
Common stock issued as penalty in connection with financing	\$ 773,958	\$		\$ 773,958
Common stock canceled-previously issued for services rendered	\$ (480,000)	\$		\$ (480,000)
Decrease in accounts receivable	\$ 9,301	\$		\$ 9,301
Increase in other assets	\$ (9,120)	\$		\$ (9,120)
Increase in due related parties	\$ 2,496	\$		\$ 2,496
Increase (decrease) in accounts payable and accrued liabilities	\$ 83,175	\$ 659,400	1	\$ 742,575
Net cash used in operating activities	\$ (1,517,623)	\$ 390,000		\$ (1,127,623)
Cash flows from investing activities:				
Capital expenditures	\$ (35,852)	\$		\$ (35,852)
Net cash used in investing activities	\$ (35,852)	\$		\$ (35,852)
Cash flows from financing activities				
Proceeds from issuance of convertible notes	\$ 1,600,000	\$ (390,000)	1c	\$ 1,210,000
Net cash provided by financing activities	\$ 1,600,000	\$ (390,000)		\$ 1,210,000
Net increase in cash and cash equivalents	\$ 46,525	\$		\$ 46,525
Cash and cash equivalents at beginning of period	\$ 31,190	\$		\$ 31,190
Cash and cash equivalents at end of period	\$ 77,715	\$		\$ 77,715



**APPLIED DNA SCIENCES, INC**  
**(a development stage company)**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**MARCH 31, 2007**  
**(Unaudited)**

**NOTE J - SUBSEQUENT EVENTS**

On April 23, 2007, the Company issued and sold a \$100,000 principal amount secured promissory note bearing interest at a rate of 10% per annum and a warrant to purchase 200,000 shares of our common stock to James A. Hayward, a director and the Chief Executive Officer of the Company.

On May 17, 2007 the Company amended its Articles of Incorporation to increase the number of authorized shares of common stock of the Company, \$0.001 par value per share, to 410,000,000 shares following stockholder approval at the annual meeting of stockholders held on May 16, 2007.

On May 16, 2007, the Company increased the number of shares under their ESOP (employee stock option program) from 16,000,000 to 20,000,000 shares following stockholder approval at the annual meeting of stockholders held on May 16, 2007.

In May 2007, the Company settled certain pending litigation and other claims arising out of certain former employees' and consultants' prior employment or consulting relationships with the Company. The Company is obligated to pay an aggregate amount of \$605,000 beginning June 1, 2007 in five monthly payments. The settlement agreements provide that each of the former employees and consultants can cause a judgment to be entered against the Company in an amount equal to three times the remaining balance due to such former employee or consultant under the applicable settlement agreement, plus interest, if the Company defaults on any payment obligation to such person and the Company does not satisfy it within the ten day period after receiving notice of such default.

## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS

The following discussion should be read in conjunction with our Consolidated Financial Statements and Notes thereto, included elsewhere within this report. The quarterly report contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, including statements using terminology such as “can”, “may”, “believe”, “designated to”, “will”, “expect”, “plan”, “anticipate”, “estimate”, “potential” or “continue”, or the negative or other comparable terminology regarding beliefs, plans, expectations or intentions regarding the future. You should read statements that contain these words carefully because they:

- discuss our future expectations;
- contain projections of our future results of operations or of our financial condition; and
- state other “forward-looking” information.

We believe it is important to communicate our expectations. However, forward looking statements involve risks and uncertainties and our actual results and the timing of certain events could differ materially from those discussed in forward-looking statements as a result of certain factors, including those set forth under “Risk Factors,” “Business” and elsewhere in this report. All forward-looking statements and risk factors included in this document are made as of the date hereof, based on information available to us as of the date thereof, and we assume no obligations to update any forward-looking statement or risk factor, unless we are required to do so by law.

### **Introduction**

We provide botanical DNA encryption, embedment and authentication solutions that can help protect companies, governments and consumers from counterfeiting, fraud, piracy, product diversion, identity theft, and unauthorized intrusion into physical locations and databases. Our SigNature Program provides a secure, accurate and cost-effective means for customers to incorporate our SigNature DNA Markers in, and then quickly and reliably authenticate and identify, a broad range of items such as artwork and collectibles, fine wine, consumer products, digital media, financial instruments, identity cards and other official documents. Having the ability to reliably authenticate and identify counterfeit versions of such items enables companies and governments to detect, deter, interdict and prosecute counterfeiting enterprises and individuals.

Our SigNature Program enables our potential clients to cost-effectively:

- assure manufacturers, suppliers, distributors, retailers and end-users that their products are authentic and can be forensically authenticated;
- integrate our SigNature DNA Markers with existing security solutions such as barcodes, radio frequency identification (RFID) tags, holograms, microchips and other securities measures; and
- add value to the “bottom-line” by helping to diminish product diversion and counterfeiting.

Counterfeit and diverted products continue to pose a significant and growing problem with consumer packaged goods, especially for prestige and established brands worldwide. Piracy, identity theft and forged documents and items are also highly prevalent in vertical markets such as digital media, fine art, luxury goods, and alcoholic beverages. Key aspects of our strategy include:

- continuing to improve and customize our solution to meet our potential customers' needs;



- continuing to develop and enhance our existing DNA marker authentication technologies;
- expanding our customer base both domestically and abroad by targeting high volume markets; and
- augmenting our competitive position through strategic acquisitions and alliances.

## **Plan of Operations**

### *General*

We expect to generate revenues principally from sales of our SigNature Program. We are currently attempting to develop business in six target markets: art and collectibles, fine wine, consumer products, digital recording media, pharmaceuticals, and homeland security. We intend to pursue both domestic and international sales opportunities in each of these vertical markets.

We believe that our existing capital resources will enable us to fund our operations until approximately July 2007. We believe we will be required to seek additional capital to sustain or expand our prototype and sample manufacturing, and sales and marketing activities, and to otherwise continue our business operations beyond that date. We have no commitments for any future funding, and may not be able to obtain additional financing or grants on terms acceptable to us, if at all, in the future. If we are unable to obtain additional capital this would restrict our ability to grow and may require us to curtail or discontinue our business operations. Additionally, while a reduction in our business operations may prolong our ability to operate, that reduction would harm our ability to implement our business strategy. If we can obtain any equity financing, it may involve substantial dilution to our then existing shareholders.

### *Product Research and Development*

We anticipate spending approximately \$200,000 for product research and development activities during the next twelve (12) months. This projected expenditure for product research and development activities is dependent upon our ability to obtain sources of financing or generate revenues. There is no guarantee that we will be successful in raising the funds required or generating revenues sufficient to fund the projected research and product development costs during the next twelve (12) months.

On March 19, 2007, we entered into a Technology Reseller Agreement (the "HPT Agreement") with HPT International, LLC ("HPT"). In the HPT Agreement we agreed to supply our SigNature DNA Markers to HPT to be affixed onto HPT's holograms, Nylon 6 tags and other plastic or metal food tags. HPT has been granted exclusive rights to affix our SigNature DNA Markers onto its tagging products for distribution to its customers in the United States in the poultry and kosher foods markets, and non-exclusive rights to attach our SigNature DNA Markers onto its tagging products for distribution to its customers worldwide. We will receive a fee for each SigNature DNA Marker that is attached to an HPT product and distributed to a third party, and for each forensic authentication test that we perform at HPT's request. HPT has been granted exclusive rights in the U.S. poultry and kosher foods markets with respect to new customers through March 18, 2008. After that date, HPT will lose its exclusive rights if it does not realize certain sales goals or does not agree to certain minimum purchases during the subsequent year of the agreement. Under the HPT Agreement, HPT has the right to permanent exclusivity in the U.S. poultry and kosher foods markets if realizes its sales goals for the first two years under the HPT Agreement and achieves an additional milestone to be agreed by us and HPT prior to March 18, 2009. The HPT Agreement may be terminated by us or HPT on any anniversary of the HPT Agreement by providing ninety (90) days prior written notice.

### *Acquisition of Plant and Equipment and Other Assets*

We do not anticipate the sale of any material property, plant or equipment during the next 12 months. We anticipate spending approximately \$200,000 on the acquisition of leasehold improvements during the next 12 months. This projected expenditure for leasehold improvements is dependent upon our ability to obtain sources of financing or generate revenues. There is no guarantee that we will be successful in raising the funds required or generating revenues sufficient to fund the projected costs of the leasehold improvements during the next 12 months.



### *Number of Employees*

We currently have seven employees and two part-time employees. We anticipate that it may become desirable to add additional full and/or part time employees to discharge certain critical functions during the next 12 months. Specifically, the company expects to increase its staffing dedicated to sales, product prototyping, manufacturing of DNA Markers and forensic authentication services. In order for us to attract and retain quality personnel, we anticipate we will have to offer competitive salaries. Any such increase in personnel is dependent upon our ability to generate sufficient revenues or obtain sources of financing. There is no guarantee that we will be successful in raising the funds required or generating revenues sufficient to fund an increase in the number of our employees. If we expand by hiring additional employees, we will incur additional costs for such personnel.

### **Critical Accounting Policies**

Financial Reporting Release No. 60, published by the Securities and Exchange Commission (“SEC”), recommends that all companies include a discussion of critical accounting policies used in the preparation of their financial statements. While all these significant accounting policies impact our financial condition and results of operations, we view certain of these policies as critical. Policies determined to be critical are those policies that have the most significant impact on our consolidated financial statements and require management to use a greater degree of judgment and estimates. Actual results may differ from those estimates.

We believe that given current facts and circumstances, it is unlikely that applying any other reasonable judgments or estimate methodologies would cause a material effect on our consolidated results of operations, financial position or liquidity for the periods presented in this report.

The accounting policies identified as critical are as follows:

- Equity issued with registration rights
- Warrant liability
- Fair value of intangible assets

### *Equity Issued with Registration Rights*

In connection with the placements of our convertible notes and warrants to certain investors during the fiscal quarters ended December 31, 2003, December 31, 2004, March 31, 2005, March 31, 2006 and June 30, 2006, we granted certain registration rights that provide for liquidated damages in the event of failure to timely perform under the agreements. Although these notes and warrants do not provide for net-cash settlement, the existence of liquidated damages provides for a defacto net-cash settlement option. Therefore, the common stock underlying the notes and warrants subject to such liquidated damages does not meet the tests required for shareholders’ equity classification, and accordingly has been reflected between liabilities and equity in the accompanying consolidated balance sheet until such time as the conditions are eliminated.

### *Warrant Liability*

In connection with the placement of certain debt instruments, as described above, we issued freestanding warrants. Although the terms of the warrants do not provide for net-cash settlement, in certain circumstances, physical or net-share settlement is deemed to not be within our control and, accordingly, we are required to account for these freestanding warrants as a derivative financial instrument liability, rather than as shareholders’ equity.



The warrant liability is initially measured and recorded at its fair value, and is then re-valued at each reporting date, with changes in the fair value reported as non-cash charges or credits to earnings. For warrant-based derivative financial instruments, the Black-Scholes option pricing model is used to value the warrant liability.

The classification of derivative instruments, including whether such instruments should be recorded as liabilities or as equity, is re-assessed at the end of each reporting period. Derivative instrument liabilities are classified in the balance sheet as current or non-current based on whether or not net-cash settlement of the derivative instrument could be required within 12 months of the balance sheet date.

We do not use derivative instruments to hedge exposures to cash flow, market, or foreign currency risks.

#### *Fair Value of Intangible Assets*

We have adopted SFAS No. 142, Goodwill and Other Intangible Assets, whereby we periodically test our intangible assets for impairment. On an annual basis, and when there is reason to suspect that their values have been diminished or impaired, these assets are tested for impairment, and write-downs will be included in results from operations. On July 12, 2005, we acquired certain intellectual properties from Biowell through an Asset Purchase Agreement in exchange for 36 million shares of our restricted common stock having an aggregate fair value at the date of issuance of \$24.12 million. The value of the acquired intangible assets was \$9,430,900, with the balance of the purchase price, or \$14,689,100, charged to operations as a cost of the transaction.

During the year ended September 30, 2006, the Company management performed an evaluation of its intangible assets (intellectual property) for purposes of determining the implied fair value of the assets at September 30, 2006. The test indicated that the recorded remaining book value of its intellectual property exceeded its fair value, as determined by discounted cash flows. As a result, upon completion of the assessment, management recorded a non-cash impairment charge of \$5,655,011, net of tax, or \$0.05 per share during the year ended September 30, 2006 to reduce the carrying value of the patents to \$2,091,800. Considerable management judgment is necessary to estimate the fair value. Accordingly, actual results could vary significantly from management's estimates.

The identifiable intangible assets acquired and their carrying values at March 31, 2007 are:

	<b>Gross Carrying Amount</b>	<b>Accumulated Amortization and Impairment Charge</b>	<b>Net</b>	<b>Residual Value</b>	<b>Weighted Average Amortization Period (Years)</b>
Amortizable Intangible Assets:					
Intellectual Property	\$ 9,430,900	\$ 7,520,996	\$ 1,909,904	—	7
Patents	34,237	21,999	12,238	—	5
Total Amortized					

Identifiable Intangible	\$ 9,465,137	\$ 7,542,995	\$ 1,922,142	—	6.99
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Total amortization expense charged to operations for the three months ended March 31, 2007 and 2006 were \$92,661 and \$677,040.

Estimated amortization expense as of March 31, 2007 is as follows:

2007	\$ 370,642
2008	370,642
2009	365,504
2010	363,791
2011	
and after	451,563
Total	\$ 1,922,142

### *Use of Estimates*

In preparing financial statements in conformity with accounting principles generally accepted in the United States of America, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and revenue and expenses during the reporting period. The most significant estimates relate to the estimation of percentage of completion on uncompleted contracts, valuation of inventory, allowance for doubtful accounts and estimated life of customer lists. Actual results could differ from those estimates.

### **Restatement of Consolidated Financial Statements**

The Company has restated its consolidated financial statements as of and for the year ended September 30, 2005 and the quarterly unaudited data for the first three quarters of 2006 and all of 2005.

These restatements and resulting revisions relate to the accounting treatment for and disclosure regarding the issuance by the Company of options and warrants to acquire the Company's common stock. In addition the Company corrected certain errors in accounting for the exchange of its common stock for previously incurred debt with a Company director. These errors were discovered in connection with comments raised by the SEC in their review and comment on the Company's Registration Statement on Form SB-2, as amended.

In this regard, you should rely on the restated financial results for the fiscal year ended September 30, 2005 and for each of the quarters in the year 2005 and the first, second and third quarters of 2006. As the Company previously reported in its Current Report on Form 8-K, dated May 16, 2006, you should not rely on the Company's previously issued consolidated financial statements and other financial information for these reporting periods.

The consolidated financial statements for the three months ended March 31, 2006 have been restated from the amounts previously reported to correct the accounting for financial derivatives. While the effect of the corrections to the financial statements is fully described in accompanying notes to the restated consolidated financial statements, the following is a summary of the net effect of the errors on these consolidated financial statements:

- the Company's net income for the three months ended March 31, 2006 decreased by \$1,330,202 from a net income of \$3,363,553 to a net income of \$2,033,351.



## **Comparison of Results of Operations for the Three Months Ended March 31, 2007 and 2006**

### **Revenues**

From our inception on September 16, 2002, we have not generated significant revenues from operations.

### **Costs and Expenses**

#### *Selling, General and Administrative*

Selling, general and administrative expenses increased from \$0.950 million for the three months ended March 31, 2006 to \$1.989 million for the three months ended March 31, 2007. This increase of \$1.04 million, or 110%, is primarily attributable to an increase in amortized loan costs expense of \$389,775 for borrowing in 2006 as well as an increase in cost incurred in connection with professional services.

#### *Research and Development*

Research and development expenses decreased from \$75,000 for the three months ended March 31, 2006 to \$39,000 for the same period in 2007. The decrease of \$36,000 is attributed to less research and development activity than the prior period.

#### *Depreciation and Amortization*

In the three months ended March 31, 2007, depreciation and amortization decreased by \$233,318 from \$341,676 to \$108,358 for the period compared to the same period in 2006. The decrease is attributable to the reduced amortization of our intellectual property due to our impairment recorded in the period ended September 30, 2006.

#### *Total Operating Expenses*

Total operating expenses increased to \$2.16 million from \$1.37 million, or an increase of \$0.77 million primarily attributable to an increase in amortized loan costs expense for borrowings in 2006 as well as an increase in costs incurred in connection with professional services.

#### *Other Income/Loss*

Loss on reevaluation of debt derivative and warrant liability increased by \$10.36 million from a gain of \$3.97 million for the three months ended March 31, 2006 to a loss of \$6.39 million for the three months ended March 31, 2007.

#### *Interest Expenses*

Interest expense for the three months ended March 31, 2007 increased by \$0.274 million to \$0.846 million from \$0.572 million in the same period of 2006. The increase in interest expense was due to the financings we effected in 2006.

#### *Net Income (loss)*

Net loss for the three months ended March 31, 2007 increased to a loss of \$9.37 million from a net income of \$2.03 million in the prior period primarily attributable to an increased loss on reevaluation of debt derivative and warrant liability.

## **Liquidity and Capital Resources**

Our liquidity needs consist of our working capital requirements, indebtedness payments and research and development expenditure funding. Historically, we have financed our operations through the sale of equity and convertible debt as well as borrowings from various credit sources.

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In fiscal 2005, we completed two private placements of convertible debt and associated warrants. In November and December, 2004 we issued and sold \$1.465 million in aggregate principal amount of promissory notes, convertible at \$0.50 per share, and associated warrants to purchase up to 2,930,000 shares of our common stock, exercisable at \$0.75 per share for three years from their date of issuance, to 13 investors (the "December 2004 Placement"). Each promissory note was automatically convertible into shares of our common stock at a price of \$0.50 per share upon the closing of a subsequent private placement by us for at least \$1 million. In January and February of 2005, we issued and sold \$7.371 million in aggregate principal amount of 10% Secured Convertible Promissory Notes, convertible at \$0.50 per share, and associated warrants to purchase up to 14,742,000 shares of our common stock, exercisable at \$0.75 per share until five years from their date of issuance, to 61 investors (the "January and February 2005 Placement"). Upon the closing of the January and February 2005 Offering, the notes issued in the December 2004 Placement automatically converted into an aggregate of 2,930,000 shares of our common stock, and upon the filing of this registration statement on February 15, 2005, the notes issued in the January and February 2005 Placement automatically converted into an aggregate of 14,742,000 shares of our common stock. Additional private placements in fiscal 2005 raised \$243,000. We also received proceeds of \$60,000 from the exercise of a warrant to purchase 100,000 shares of our common stock in fiscal 2005. The \$9.135 million in gross proceeds from these private placements and warrant exercises were used to fund commissions, fees and expenses associated with the placements, consultants and public reporting costs, salaries and wages, royalties, research and development, facility costs as well as general working capital needs. Since the conversion price of the notes issued in the November and December 2003, December 2004, December 2005 and the January and February 2005 placements were less than the market price of our common stock at the time these notes were issued, we recognized a charge relating to the beneficial conversion feature of these notes during the quarter in which they are issued.

In fiscal 2006, we completed three additional private placements of convertible debt and associated warrants. On November 3, 2005, we issued and sold a promissory note in the principal amount of \$550,000 to Allied International Fund, Inc. ("Allied"). Allied in turn financed a portion of the making of this loan by borrowing \$450,000 from certain persons, including \$100,000 from James A. Hayward, a director and our Chief Executive Officer. The terms of the promissory note provided that we issue upon the funding of the note warrants to purchase 5,000,000 shares of our common stock at an exercise price of \$0.50 per share to certain persons designated by Allied. On November 9, 2005, we issued nine warrants to Allied and eight other persons to purchase an aggregate of 5,500,000 shares of our common stock at an exercise price of \$0.50 per share. These warrants included a warrant to purchase 1,100,000 shares that was issued to James A. Hayward, a director and our Chief Executive Officer. We paid \$55,000 in cash to VC Arjent, Ltd. for its services as the placement agent with respect to this placement. All principal and accrued but unpaid interest under the promissory note was paid in full shortly after the closing of and from the proceeds of a private placement we completed on March 8, 2006. On March 8, 2006, we issued and sold an aggregate of 30 units consisting of (i) a \$50,000 principal amount secured convertible promissory note bearing interest at 10% per annum and convertible at \$0.50 per share, and (ii) a warrant to purchase 100,000 shares of our common stock at an exercise price of \$0.50 per share, for aggregate gross proceeds of \$1.5 million. The units were sold pursuant to subscription agreements by and between each of the purchasers and Applied DNA Operations Management, Inc., a Nevada corporation and our wholly owned subsidiary (our "Subsidiary"). The \$2.050 million in gross proceeds from these first two offerings were held by our Subsidiary for our benefit and used to fund commissions, fees and expenses associated with the placements, to repay the outstanding promissory note described above plus accrued interest thereunder, to fund financing fees, consultants and public reporting costs, salaries and wages, research and development, facility costs as well as and general working capital needs. On March 24, 2006, we commenced an offering (the "Offshore Offering") of up to 140 units, at a price of \$50,000 per unit, for a maximum offering of \$7 million for sale to "accredited investors" who are not "U.S. persons." The units being sold as part of the Offshore Offering consist of (i) a \$50,000 principal amount secured convertible promissory note, and (ii) a warrant to purchase 100,000 shares of our common stock at a price of \$0.50 per share. On May 2, 2006, we closed on the first tranche of the Offshore Offering in which we sold 20 units for aggregate gross proceeds of \$1,000,000. We paid Arjent Limited \$375,000 in commissions, fees and expenses from these gross proceeds. On June 15, 2006, we completed the second tranche of the Offshore Offering in which we sold 59 units for aggregate gross proceeds of \$2,950,000. We paid Arjent Limited \$442,500 in

commissions, fees and expenses from these gross proceeds. Additionally, on July 10, 2006 we issued 2.4 million shares of our common stock to Arjent Limited at \$0.001 per share as partial consideration for its services in connection with the Offshore Offering.

On March 29, 2006 and April 13, 2006, we borrowed \$200,000 in the aggregate, at a rate of 7.5% per annum, from BioCogent whose President and Chief Executive Officer and sole stockholder is James A. Hayward, one of our directors and our Chief Executive Officer. These loans were due and payable upon the earlier to occur of (1) the close of business on June 30, 2006, or (2) the closing of the issuance and sale of our securities for gross proceeds of at least \$250,000. The proceeds from the loans were used for general corporate purposes. The note issued on March 29, 2006 was repaid with interest in May, 2006. The note issued on April 13, 2006 was repaid with interest in June, 2006.

On April 23, 2007, we issued and sold a \$100,000 principal amount secured promissory note bearing interest at a rate of 10% per annum and a warrant to purchase 200,000 shares of our common stock to James A. Hayward, a director and the Chief Executive Officer of the Company. The promissory note and accrued but unpaid interest thereon are convertible into shares of common stock of the Company at a price of \$0.50 per share by the holder of the promissory note at any time from April 23, 2007, through April 22, 2008, and shall automatically convert on April 22, 2008 at a conversion price of \$0.15. At any time prior to conversion, we have the right to prepay the promissory note and accrued but unpaid interest thereon upon 3 days prior written notice (during which period the holder can elect to convert the note). Until the principal and interest under the promissory note is paid in full, or converted into our common stock, the promissory note will be secured by a security interest in all of our assets. This security interest is pari passu with the security interest granted to the holders of \$1,500,000 in aggregate principal amount secured convertible promissory notes of the Company issued on March 8, 2006, and the holders of \$3,950,000 in aggregate principal amount secured convertible promissory notes of the Company issued on May 2, 2006 and June 15, 2006. The warrant is exercisable for a four-year period commencing on April 23, 2008, and expiring on April 22, 2012, at a price of \$0.50 per share. The warrant may be redeemed at our option at a redemption price of \$0.001 upon the earlier of (i) April 22, 2010, and (ii) the date our common stock has traded on The Over the Counter Bulletin Board at or above \$1.00 per share for 20 consecutive trading days.

As of March 31, 2007, we had \$5,450,000 in outstanding notes payable. Please see “Management’s Discussion and Analysis — Liquidity and Capital Resources” and Note C to the financial statements in this quarterly report for a full description of the terms of the outstanding promissory notes.

Substantially all of the real property used in our business is leased under operating lease agreements.

As of March 31, 2007, we had a working capital deficit of approximately \$1.27 million. For the six months ended March 31, 2007, we generated a net cash flow deficit from operating activities of \$1.1 million consisting primarily of year to date losses of \$10.04 million. Non-cash adjustments included \$2,162,910 in depreciation and amortization charges and a non-cash increase of \$4,289,290 attributable to the repricing of the debt derivative and warrant liability. Additionally, we had a net decrease in current assets of \$98,050 and a net increase in current liabilities of \$2,366,177. Cash used in investing activities totaled \$11,039, which was utilized for acquisition of property and equipment. We did not have any cash provided by financing activities for the six months ended March 31, 2007.

From our inception on September 16, 2002 through March 31, 2007, we generated a cash flow deficit of \$16,744,194 from operating activities. Cash flows used in investing activities was \$214,058 during this period. We met our cash requirements during this period through the private placement of \$432,000 of common stock, \$13,446,500 from the issuance of convertible notes, \$2,850,088 from the issuance of notes payable (net of repayments and costs) and \$343,750 from the proceeds from the exercise of options to acquire our common stock.

We expect capital expenditures to be less than \$200,000 in fiscal 2007. Our primary investments will be in laboratory equipment to support prototyping and our authentication services.

We currently require additional financing in order to meet our current and projected cash flow deficits from operations and development. We presently do not have any available credit, bank financing or other readily available external sources of liquidity. Financing transactions may include the issuance of equity or debt securities, obtaining credit facilities, or other financing mechanisms. However, the trading price of our common stock, a downturn in the U.S. or global stock and debt markets and other reasons could make it more difficult to obtain financing through the issuance of equity securities or borrowing. Further, if we issue additional equity or convertible debt securities, stockholders may experience additional dilution or the new equity securities may have rights, preferences or privileges senior to those of existing holders of our common stock. If additional financing is not available or is not available on acceptable terms, this could have a material adverse effect on our business, results of operations liquidity and financial condition.

Our registered independent certified public accountants have stated in their report dated January 5, 2007, that we have incurred operating losses in the last two years, and that we are dependent upon management's ability to develop profitable operations. These factors among others may raise substantial doubt about our ability to continue as a going concern.

Pursuant to the terms of a registration rights agreement with respect to common stock underlying convertible notes and warrants we issued in private placements in November and December 2003, December 2004, and January and February, 2005, if we did not have a registration statement registering the shares underlying these convertible notes and warrants declared effective on or before June 15, 2005, we are obligated to pay liquidated damages in the amount of 3.5% per month of the face amount of the notes, which equals \$367,885, until the registration statement is declared effective. At our option, these liquidated damages can be paid in cash or restricted shares of our common stock. To date we have decided to pay certain of these liquidated damages in common stock, although any future payments of liquidated damages may, at our option, be made in cash. If we decide to pay such liquidated damages in cash, we would be required to use our limited working capital and potentially raise additional funds. If we decide to pay the liquidated damages in shares of common stock, the number of shares issued would depend on our stock price at the time that payment is due. Based on the closing market prices of \$0.66, \$0.58, \$0.70, \$0.49, \$0.32 and \$0.20 for our common stock on July 15, 2005, August 15, 2005, September 15, 2005, October 17, 2005, November 15, 2005 and December 15, 2005, respectively, we issued a total of 3,807,375 shares of common stock in liquidated damages from August, 2005 to January, 2006 to persons who invested in the January and February, 2005 private placements. The issuance of shares upon any payment by us of further liquidated damages will have the effect of further diluting the proportionate equity interest and voting power of holders of our common stock, including investors in this offering.

We paid liquidated damages in the form of common stock only for the period from June 15, 2005 to December 15, 2005, and only to persons who invested in the January and February, 2005 private placements. We believe that we have no enforceable obligation to pay liquidated damages to holders of any shares we agreed to register under the registration rights agreement for periods after the first anniversary of the date of issuance of such shares, since they were eligible for resale under Rule 144 of the Securities Act during such periods, and such liquidated damages are grossly inconsistent with actual damages to such persons. Nonetheless, as of March 31, 2007 we have accrued approximately \$6.2 million in penalties representing further liquidated damages associated with our failure to have the registration statement declared effective by the deadline, and have included this amount in accounts payable and accrued expenses.

In May 2007, we settled certain pending litigation and all other claims arising out of certain former employees' and consultants' prior employment or consulting relationships with us. We agreed to pay the former employees and consultants an aggregate amount of \$605,000 in cash in five equal installments due on the first day of each month over the five month period beginning on June 1, 2007. The settlement agreements provide that each of the former employees and consultants can cause a judgment to be entered against us, APDN (B.V.I.) Inc. and Applied DNA Operations Management, Inc. in an amount equal to three times the remaining balance due to such former employee or consultant under the applicable settlement agreement, plus interest, if we default on any payment obligation to such person and we do not satisfy it within the ten day period after receiving notice of such default.

### **Off-Balance Sheet Arrangements**

We do not have any off-balance sheet arrangements.

### **Inflation**

The impact of inflation on the costs of the Company is dependent upon market conditions. The Company is not aware of any inflationary pressures that have had any significant impact on the Company's operations over the past quarter, and the Company does not anticipate that inflationary factors will have a significant impact on future operations.

### **Going Concern**

The financial statements included in this filing have been prepared in conformity with generally accepted accounting principles that contemplate our continuance as a going concern. Our auditors, in their report dated January 5, 2007, have expressed substantial doubt about our ability to continue as going concern. Our cash position may be inadequate to pay all of the costs associated with the testing, production and marketing of our products. Management intends to use borrowings and the sale of equity or convertible debt to mitigate the effects of its cash position, however no assurance can be given that debt or equity financing, if and when required will be available. The financial statements do not include any adjustments relating to the recoverability and classification of recorded assets and classification of liabilities that might be necessary should we be unable to continue existence.

## **RISK FACTORS**

Because of the following factors, as well as other variables affecting our operating results and financial condition, past financial performance may not be a reliable indicator of future performance, and historical trends should not be used to anticipate results or trends in future periods.

### **If We Are Unable to Obtain Additional Financing Our Business Operations Will be Harmed or Discontinued, and If We Do Obtain Additional Financing Our Shareholders May Suffer Substantial Dilution.**

We believe that our existing capital resources will enable us to fund our operations until approximately July 2007. We will be required to seek additional capital to sustain or expand our prototype and sample manufacturing, and sales and marketing activities, and to otherwise continue our business operations beyond that date. We have no commitments for any future funding, and may not be able to obtain additional financing or grants on terms acceptable to us, if at all, in the future. If we are unable to obtain additional capital this would restrict our ability to grow and may require us to curtail or discontinue our business operations. Additionally, while a reduction in our business operations may prolong our ability to operate, that reduction would harm our ability to implement our business strategy. If we can obtain any equity financing, it may involve substantial dilution to our then existing shareholders.

### **We Have a History Of Losses Which May Continue, and Which May Harm Our Ability to Obtain Financing and Continue Our Operations.**





We incurred net losses of \$2.4 million for the year ended September 30, 2006. For the three months ended March 31, 2007, we incurred a net loss of \$9,370,238. These net losses have principally been the result of the various costs associated with our selling, general and administrative expenses as we commenced operations, acquired, developed and validated technologies, began marketing activities, and our interest expense on notes and warrants we issued to obtain financing. Our operations are subject to the risks and competition inherent in a company moving from the development stage to a new growth enterprise. We may not generate sufficient revenues from operations to achieve or sustain profitability on a quarterly, annual or any other basis in the future. Our revenues and profits, if any, will depend upon various factors, including whether our existing products and services or any new products and services we develop will achieve any level of market acceptance. If we continue to incur losses, our accumulated deficit will continue to increase, which might significantly impair our ability to obtain additional financing. As a result, our business, results of operations and financial condition would be significantly harmed, and we may be required to reduce or terminate our operations.

**Our Independent Auditors Have Expressed Substantial Doubt About Our Ability to Continue As a Going Concern, Which May Hinder Our Ability to Obtain Future Financing.**

In their report dated January 5, 2007, our independent auditors stated that our financial statements for the year ended September 30, 2006 were prepared assuming that we would continue as a going concern, and that they have substantial doubt about our ability to continue as a going concern. Our auditors' doubts are based on our incurring net losses of \$93 million during the period from September 16, 2002 (date of inception) to September 30, 2006. We continue to experience net operating losses. Our ability to continue as a going concern is subject to our ability to generate a profit and/or obtain necessary funding from outside sources, including by the sale of our securities, obtaining loans from financial institutions, or obtaining grants from various organizations or governments, where possible. Our continued net operating losses and our auditors' doubts increase the difficulty of our meeting such goals and our efforts to continue as a going concern may not prove successful.

**We have a Short Operating History, a Relatively New Business Model, and Have Not Produced Significant Revenues. This Makes it Difficult to Evaluate Our Future Prospects and Increases the Risk That We Will Not Be Successful.**

We have a short operating history with our current business model, which involves the marketing, sale and distribution of botanical DNA encryption, embedment and authentication products and services. We acquired technologies upon which these products and services are based from Biowell Technology, Inc. ("Biowell") on July 12, 2005. We first derived revenue from this model in the second calendar quarter of 2006, which was insignificant. Prior to the July 12, 2005 acquisition, our operations consisted principally of providing marketing and business development services to Biowell. As a result, we have a very limited operating history for you to evaluate in assessing our future prospects. We are in the process of transitioning from a developmental stage to an early-stage growth enterprise. Our operations since inception have not produced significant revenues, and may not produce significant revenues in the near term, or at all, which may harm our ability to obtain additional financing and may require us to reduce or discontinue our operations. If we create revenues in the future, prior to our introduction of any new products, we will derive all such revenues from the sale of botanical DNA encryption, encapsulation, embedment and authentication products and services, which is an immature industry. You must consider our business and prospects in light of the risks and difficulties we will encounter as an early-stage company in a new and rapidly evolving industry. We may not be able to successfully address these risks and difficulties, which could significantly harm our business, operating results, and financial condition.

**We Are Obligated to Pay Liquidated Damages As a Result of Our Failure to Have the Registration Statement on Form SB-2 Declared Effective Prior to June 15, 2005, and any Payment of Liquidated Damages Will Either Result in Depletion of Our Limited Working Capital or Issuance of Shares of Common Stock Which Would Cause Dilution to Our Existing Shareholders.**



Pursuant to the terms of a registration rights agreement with respect to common stock underlying convertible notes and warrants we issued in private placements in November and December, 2003, December, 2004, and January and February, 2005, if we did not have a registration statement registering the shares underlying these convertible notes and warrants declared effective on or before June 15, 2005, we are obligated to pay liquidated damages in the amount of 3.5% per month of the face amount of the notes, which equals \$367,885, until the registration statement is declared effective. At our option, these liquidated damages can be paid in cash or restricted shares of our common stock. To date we have decided to pay certain of these liquidated damages in common stock, although any future payments of liquidated damages may, at our option, be made in cash. If we decide to pay such liquidated damages in cash, we would be required to use our limited working capital and potentially raise additional funds. If we decide to pay the liquidated damages in shares of common stock, the number of shares issued would depend on our stock price at the time that payment is due. Based on the closing market prices of \$0.66, \$0.58, \$0.70, \$0.49, \$0.32 and \$0.20 for our common stock on July 15, 2005, August 15, 2005, September 15, 2005, October 17, 2005, November 15, 2005 and December 15, 2005, respectively, we issued a total of 3,807,375 shares of common stock in liquidated damages from August, 2005 to January, 2006 to persons who invested in the January and February, 2005 private placements. The issuance of shares upon any payment by us of further liquidated damages will have the effect of further diluting the proportionate equity interest and voting power of holders of our common stock, including investors in this offering.

We paid liquidated damages in the form of common stock only for the period from June 15, 2005 to December 15, 2005, and only to persons who invested in the January and February, 2005 private placements. We believe that we have no enforceable obligation to pay liquidated damages to holders of any shares we agreed to register under the registration rights agreement for periods after the first anniversary of the date of issuance of such shares, since they were eligible for resale under Rule 144 of the Securities Act during such periods, and such liquidated damages are grossly inconsistent with actual damages to such persons. Nonetheless, as of March 31, 2007 we have accrued approximately \$6.2 million in penalties representing further liquidated damages associated with our failure to have the registration statement declared effective by the deadline, and have included this amount in accounts payable and accrued expenses.

**If Our Existing Products and Services are Not Accepted by Potential Customers or We Fail to Introduce New Products and Services, Our Business, Results of Operations and Financial Condition Will be Harmed.**

There has been limited market acceptance of our botanical DNA encryption, encapsulation, embedment and authentication products and services to date. Some of the factors that will affect whether we achieve market acceptance of our solutions include:

- availability, quality and price relative to competitive solutions;
- customers' opinions of the solutions' utility;
- ease of use;
- consistency with prior practices;
- scientists' opinions of the solutions' usefulness;
- citation of the solutions in published research; and
- general trends in anti-counterfeit and security solutions' research.

The expenses or losses associated with the continued lack of market acceptance of our solutions will harm our business, operating results and financial condition.



Rapid technological changes and frequent new product introductions are typical for the markets we serve. Our future success may depend in part on continuous, timely development and introduction of new products that address evolving market requirements. We believe successful new product introductions may provide a significant competitive advantage because customers invest their time in selecting and learning to use new products, and are often reluctant to switch products. To the extent we fail to introduce new and innovative products, we may lose any market share we then have to our competitors, which will be difficult or impossible to regain. Any inability, for technological or other reasons, to successfully develop and introduce new products could reduce our growth rate or damage our business. We may experience delays in the development and introduction of products. We may not keep pace with the rapid rate of change in anti-counterfeiting and security products' research, and any new products acquired or developed by us may not meet the requirements of the marketplace or achieve market acceptance.

**If We Are Unable to Retain the Services of Drs. Hayward or Liang We May Not Be Able to Continue Our Operations.**

Our success depends to a significant extent upon the continued service Dr. James A. Hayward, our Chief Executive Officer; and Dr. Benjamin Liang, our Secretary and Strategic Technology Development Officer. We do not have employment agreements with Drs. Hayward or Liang. Loss of the services of Drs. Hayward or Liang could significantly harm our business, results of operations and financial condition. We do not maintain key-man insurance on the lives of Drs. Hayward or Liang.

**The Markets for our SigNature Program are Very Competitive, and We May be Unable to Continue to Compete Effectively in this Industry in the Future.**

The principal markets for our SigNature Program are intensely competitive. We compete with many existing suppliers and new competitors continue to enter the market. Many of our competitors, both in the United States and elsewhere, are major pharmaceutical, chemical and biotechnology companies, or have strategic alliances with such companies, and many of them have substantially greater capital resources, marketing experience, research and development staff, and facilities than we do. Any of these companies could succeed in developing products that are more effective than the products that we have or may develop and may be more successful than us in producing and marketing their existing products. Some of our competitors that operate in the anti-counterfeiting and fraud prevention markets include: Applied Optical Technologies, Authentix, Biowell, ChemTAG, Collectors Universe Inc., Collotype, Data Dot Technology, Digimarc Corp., DNA Technologies, Inc., Informium AG, Inksure Technologies, L-1 Identity Solutions, Manakoa, SmartWater Technology, SureTrace, Tracetag and Warnex.

We expect this competition to continue and intensify in the future. Competition in our markets is primarily driven by:

- product performance, features and liability;
- price;
- timing of product introductions;
- ability to develop, maintain and protect proprietary products and technologies;
- sales and distribution capabilities;
- technical support and service;
- brand loyalty;
- applications support; and
- breadth of product line.

If a competitor develops superior technology or cost-effective alternatives to our products, our business, financial condition and results of operations could be significantly harmed.



**We Need to Expand Our Sales, Marketing and Support Organizations and Our Distribution Arrangements to Increase Market Acceptance of Our Products and Services.**

We currently have few sales, marketing, customer service and support personnel and will need to increase our staff to generate a greater volume of sales and to support any new customers or the expanding needs of existing customers. The employment market for sales, marketing, customer service and support personnel in our industry is very competitive, and we may not be able to hire the kind and number of sales, marketing, customer service and support personnel we are targeting. Our inability to hire qualified sales, marketing, customer service and support personnel may harm our business, operating results and financial condition. We do not currently have any arrangements with any distributors and we may not be able to enter into arrangements with qualified distributors on acceptable terms or at all. If we are not able to develop greater distribution capacity, we may not be able to generate sufficient revenue to support our operations.

**Failure to License New Technologies Could Impair Sales of Our Existing Products or Any New Product Development We Undertake in the Future.**

To generate broad product lines, it is advantageous to sometimes license technologies from third parties rather than depend exclusively on the development efforts of our own employees. As a result, we believe our ability to license new technologies from third parties is and will continue to be important to our ability to offer new products. In addition, from time to time we are notified or become aware of patents held by third parties that are related to technologies we are selling or may sell in the future. After a review of these patents, we may decide to seek a license for these technologies from these third parties. There can be no assurance that we will be able to successfully identify new technologies developed by others. Even if we are able to identify new technologies of interest, we may not be able to negotiate a license on favorable terms, or at all. If we lose the rights to patented technology, we may need to discontinue selling certain products or redesign our products, and we may lose a competitive advantage. Potential competitors could license technologies that we fail to license and potentially erode our market share for certain products. Intellectual property licenses would typically subject us to various commercialization, sublicensing, minimum payment, and other obligations. If we fail to comply with these requirements, we could lose important rights under a license. In addition, certain rights granted under the license could be lost for reasons beyond our control, and we may not receive significant indemnification from a licensor against third party claims of intellectual property infringement.

**Our Failure To Manage Our Growth In Operations and Acquisitions of New Product Lines and New Businesses Could Harm our Business.**

Any growth in our operations, if any, will place a significant strain on our current management resources. To manage such growth, we would need to improve our:

- operations and financial systems;
- procedures and controls; and
- training and management of our employees.

Our future growth, if any, may be attributable to acquisitions of new product lines and new businesses. Future acquisitions, if successfully consummated, would likely create increased working capital requirements, which would likely precede by several months any material contribution of an acquisition to our net income. Our failure to manage growth or future acquisitions successfully could seriously harm our operating results. Also, acquisition costs could cause our quarterly operating results to vary significantly. Furthermore, our stockholders would be diluted if we financed the acquisitions by incurring convertible debt or issuing securities.





Although we currently only have operations within the United States, if we were to acquire an international operation; we would face additional risks, including:

- difficulties in staffing, managing and integrating international operations due to language, cultural or other differences;
- different or conflicting regulatory or legal requirements;
- foreign currency fluctuations; and
- diversion of significant time and attention of our management.

**Failure to Attract and Retain Qualified Scientific, Production and Managerial Personnel Could Harm Our Business.**

Recruiting and retaining qualified scientific and production personnel to perform and manage prototype, sample, and product manufacturing and business development personnel to conduct business development are critical to our success. In addition, our desired growth and expansion into areas and activities requiring additional expertise, such as clinical testing, government approvals, production, and marketing will require the addition of new management personnel and the development of additional expertise by existing management personnel. Because the industry in which we compete is very competitive, we face significant challenges attracting and retaining a qualified personnel base. Although we believe we have been and will be able to attract and retain these personnel, we may not be able to continue to successfully attract qualified personnel. The failure to attract and retain these personnel or, alternatively, to develop this expertise internally would harm our business since our ability to conduct business development and manufacturing will be reduced or eliminated, resulting in lower revenues. We generally do not enter into employment agreements requiring our employees to continue in our employment for any period of time.

**Our Intellectual Property Rights Are Valuable, and Any Inability to Protect Them Could Reduce the Value of Our Products, Services and Brand.**

Our patents, trademarks, trade secrets, copyrights and all of our other intellectual property rights are important assets for us. There are events that are outside of our control that pose a threat to our intellectual property rights as well as to our products and services. For example, effective intellectual property protection may not be available in every country in which our products and services are distributed. The efforts we have taken to protect our proprietary rights may not be sufficient or effective. Any significant impairment of our intellectual property rights could harm our business or our ability to compete. Protecting our intellectual property rights is costly and time consuming. Any increase in the unauthorized use of our intellectual property could make it more expensive to do business and harm our operating results. Although we seek to obtain patent protection for our innovations, it is possible we may not be able to protect some of these innovations. Given the costs of obtaining patent protection, we may choose not to protect certain innovations that later turn out to be important. There is always the possibility that the scope of the protection gained from one of our issued patents will be insufficient or deemed invalid or unenforceable. We also seek to maintain certain intellectual property as trade secrets. The secrecy could be compromised by third parties, or intentionally or accidentally by our employees, which would cause us to lose the competitive advantage resulting from these trade secrets.

**Intellectual Property Litigation Could Harm Our Business.**

Litigation regarding patents and other intellectual property rights is extensive in the biotechnology industry. In the event of an intellectual property dispute, we may be forced to litigate. This litigation could involve proceedings instituted by the U.S. Patent and Trademark Office or the International Trade Commission, as well as proceedings brought directly by affected third parties. Intellectual property litigation can be extremely expensive, and these expenses, as well as the consequences should we not prevail, could seriously harm our business.



If a third party claims an intellectual property right to technology we use, we might need to discontinue an important product or product line, alter our products and processes, pay license fees or cease our affected business activities. Although we might under these circumstances attempt to obtain a license to this intellectual property, we may not be able to do so on favorable terms, or at all. Furthermore, a third party may claim that we are using inventions covered by the third party's patent rights and may go to court to stop us from engaging in our normal operations and activities, including making or selling our product candidates. These lawsuits are costly and could affect our results of operations and divert the attention of managerial and technical personnel. A court may decide that we are infringing the third party's patents and would order us to stop the activities covered by the patents. In addition, a court may order us to pay the other party damages for having violated the other party's patents. The biotechnology industry has produced a proliferation of patents, and it is not always clear to industry participants, including us, which patents cover various types of products or methods of use. The coverage of patents is subject to interpretation by the courts, and the interpretation is not always uniform. If we are sued for patent infringement, we would need to demonstrate that our products or methods of use either do not infringe the patent claims of the relevant patent and/or that the patent claims are invalid, and we may not be able to do this. Proving invalidity, in particular, is difficult since it requires a showing of clear and convincing evidence to overcome the presumption of validity enjoyed by issued patents.

Because some patent applications in the United States may be maintained in secrecy until the patents are issued, because patent applications in the United States and many foreign jurisdictions are typically not published until eighteen months after filing, and because publications in the scientific literature often lag behind actual discoveries, we cannot be certain that others have not filed patent applications for technology covered by our or our licensor's issued patents or pending applications or that we or our licensors were the first to invent the technology. Our competitors may have filed, and may in the future file, patent applications covering technology similar to ours. Any such patent application may have priority over our or our licensors' patent applications and could further require us to obtain rights to issued patents covering such technologies. If another party has filed a United States patent application on inventions similar to ours, we may have to participate in an interference proceeding declared by the United States Patent and Trademark Office to determine priority of invention in the United States. The costs of these proceedings could be substantial, and it is possible that such efforts would be unsuccessful, resulting in a loss of our United States patent position with respect to such inventions.

Some of our competitors may be able to sustain the costs of complex patent litigation more effectively than we can because they have substantially greater resources. In addition, any uncertainties resulting from the initiation and continuation of any litigation could have a material adverse effect on our ability to raise the funds necessary to continue our operations.

#### **Accidents Related to Hazardous Materials Could Adversely Affect Our Business.**

Some of our operations require the controlled use of hazardous materials. Although we believe our safety procedures comply with the standards prescribed by federal, state, local and foreign regulations, the risk of accidental contamination of property or injury to individuals from these materials cannot be completely eliminated. In the event of an accident, we could be liable for any damages that result, which could seriously damage our business and results of operations.

#### **Potential Product Liability Claims Could Affect Our Earnings and Financial Condition.**

We face a potential risk of liability claims based on our products and services, and we have faced such claims in the past. Though we have product liability insurance coverage which we believe is adequate, we may not be able to maintain this insurance at reasonable cost and on reasonable terms. We also cannot assure that this insurance, if obtained, will be adequate to protect us against a product liability claim, should one arise. In the event that a product liability claim is successfully brought against us, it could result in a significant decrease in our liquidity or assets, which could result in the reduction or termination of our business.



**Litigation Generally Could Affect Our Financial Condition and Results of Operations.**

We generally may be subject to claims made by and required to respond to litigation brought by customers, former employees, former officers and directors, former distributors and sales representatives, and vendors and service providers. We have faced such claims and litigation in the past and we cannot assure that we will not be subject to claims in the future. In the event that a claim is successfully brought against us, considering our lack of revenue and the losses our business has incurred for the period from our inception to June 30, 2006, this could result in a significant decrease in our liquidity or assets, which could result in the reduction or termination of our business.

**Any Default on Payments Due under Settlement Agreements with Former Employees and Consultants Could Affect Our Financial Condition and Results of Operations**

In May 2007, we settled certain pending litigation and all other claims arising out of certain former employees' and consultants' prior employment or consulting relationships with us. We agreed to pay the former employees and consultants an aggregate amount of \$605,000 in cash in five equal installments due on the first day of each month over the five month period beginning on June 1, 2007.

The settlement agreements provide that each of the former employees and consultants can cause a judgment to be entered against us, APDN (B.V.I.) Inc. and Applied DNA Operations Management, Inc. in an amount equal to three times the remaining balance due to such former employee or consultant under the applicable settlement agreement, plus interest, if we default on any payment obligation to such person and we do not satisfy it within the ten day period after receiving notice of such default.

**Matter Voluntarily Reported to the Securities and Exchange Commission**

During the months of March, May, July and August 2005, we issued a total of 8,550,000 shares of our common stock to certain employees and consultants pursuant to the 2005 Incentive Stock Plan. We engaged our outside counsel to conduct an investigation of the circumstances surrounding the issuance of these shares. On April 26, 2006, we voluntarily reported the findings from this investigation to the SEC, and agreed to provide the SEC with further information arising from the investigation. We believe that the issuance of 8,000,000 shares to employees in July 2005 was effectuated by both our former President and our former Chief Financial Officer/Chief Operating Officer without approval of our board of directors. These former officers received a total of 3,000,000 of these shares. In addition, it appears that the 8,000,000 shares issued in July 2005, as well as an additional 550,000 shares issued to employees and consultants in March, May and August 2005, were improperly issued without a restrictive legend stating that the shares could not be resold legally except in compliance with the Securities Act of 1933, as amended. The members of the Company's management who effectuated the stock issuances no longer work for the Company. These shares were not registered under the Securities Act of 1933, or the securities laws of any state, and we believe that certain of these shares may have been sold on the open market, though we have been unable to determine the magnitude of such sales. If violations of securities laws occurred in connection with the resale of certain of these shares, the employees and consultants or persons who purchased shares from them may have rights to have their purchase rescinded or other claims against us for violation of securities laws, which could harm our business, results of operations, and financial condition.

**There Are a Large Number of Shares Underlying Our Options and Warrants That May be Available for Future Sale and the Sale of These Shares May Depress the Market Price of Our Common Stock and Will Cause Immediate and Substantial Dilution to Our Existing Stockholders.**

As of May 15, 2007, we had approximately 130,808,137 shares of common stock issued and outstanding and outstanding options and warrants to purchase 77,644,464 shares of common stock. All of the shares issuable upon exercise of our options and warrants may be sold without restriction. The sale of these shares may adversely affect the

market price of our common stock. The issuance of shares upon exercise of options and warrants will cause immediate and substantial dilution to the interests of other stockholders since the selling stockholders may convert and sell the full amount issuable on exercise.

**If We Fail to Remain Current on Our Reporting Requirements, We Could be Removed From the OTC Bulletin Board Which Would Limit the Ability of Broker-Dealers to Sell Our Securities and the Ability of Stockholders to Sell Their Securities in the Secondary Market.**

Companies trading on The Over The Counter Bulletin Board (the “OTC Bulletin Board”), such as us, must be reporting issuers under Section 12 or Section 15(d) of the Securities Exchange Act of 1934, as amended, and must be current in their reports under Section 13, in order to maintain price quotation privileges on the OTC Bulletin Board. If we fail to remain current on our reporting requirements, we could be removed from the OTC Bulletin Board. As a result, the market liquidity for our securities could be severely adversely affected by limiting the ability of broker-dealers to sell our securities and the ability of stockholders to sell their securities in the secondary market. Prior to May 2001, we were delinquent in our reporting requirements, having failed to file our quarterly and annual reports for the years ended 1998 - 2000 (except the quarterly reports for the first two quarters of 1999). We have been current in our reporting requirements for the last six years, however, there can be no assurance that in the future we will always be current in our reporting requirements.

**Our Common Stock is Subject to the “Penny Stock” Rules of the SEC and the Trading Market in Our Securities is Limited, Which Makes Transactions in Our Stock Cumbersome and May Reduce the Value of an Investment in Our Stock.**

The SEC has adopted Rule 15g-9 which establishes the definition of a “penny stock,” for the purposes relevant to us, as any equity security that has a market price of less than \$5.00 per share or with an exercise price of less than \$5.00 per share, subject to certain exceptions. For any transaction involving a penny stock, unless exempt, the rules require:

- that a broker or dealer approve a person’s account for transactions in penny stocks; and
- the broker or dealer receive from the investor a written agreement to the transaction, setting forth the identity and quantity of the penny stock to be purchased.

In order to approve a person’s account for transactions in penny stocks, the broker or dealer must:

- obtain financial information and investment experience objectives of the person; and
- make a reasonable determination that the transactions in penny stocks are suitable for that person and the person has sufficient knowledge and experience in financial matters to be capable of evaluating the risks of transactions in penny stocks.

The broker or dealer must also deliver, prior to any transaction in a penny stock, a disclosure schedule prescribed by the SEC relating to the penny stock market, which, in highlight form:

- sets forth the basis on which the broker or dealer made the suitability determination; and
- that the broker or dealer received a signed, written agreement from the investor prior to the transaction.

Generally, brokers may be less willing to execute transactions in securities subject to the “penny stock” rules. This may make it more difficult for investors to dispose of our common stock and cause a decline in the market value of our stock.

Disclosure also has to be made about the risks of investing in penny stocks in both public offerings and in secondary trading and about the commissions payable to both the broker-dealer and the registered representative, current quotations for the securities and the rights and remedies available to an investor in cases of fraud in penny stock

transactions. Finally, monthly statements have to be sent disclosing recent price information for the penny stock held in the account and information on the limited market in penny stocks.

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### ITEM 3. CONTROLS AND PROCEDURES

a) *Evaluation of Disclosure Controls and Procedures:* As of March 31, 2007, our management carried out an evaluation, under the supervision of the Company's Chief Executive Officer (who is its principal executive officer and principal financial officer), of the effectiveness of the design and operation of the Company's system of disclosure controls and procedures pursuant to the Securities and Exchange Act and Rules 13a-15(e) and 15d-15(e) thereunder. Based upon that evaluation, the Company's Chief Executive Officer concluded that the Company's disclosure controls and procedures were not effective, as of the date of their evaluation, for the purposes of recording, processing, summarizing and timely reporting material information required to be disclosed in reports filed by the Company under the Securities Exchange Act of 1934.

As previously disclosed in our Current Reports on Form 8-K, filed on May 18, 2006 and October 2, 2006, as a result of comments raised by the SEC, we determined that accounting errors were made in connection with

- accounting for and disclosing the fair value of warrants and options to acquire our common stock issued to non-employees as a current period expense;
- accounting for and disclosing the fair value of shares issued to a former Director in exchange for previously incurred debt;
- accounting for and disclosing the fair value of warrants issued to note holders and consultants having registration rights; and
- accounting for and disclosing the revaluation for warrant liabilities as of each reporting period.

Based on the impact of the aforementioned accounting errors, we determined to restate our consolidated financial statements as of September 30, 2005 and for the year ended September 30, 2005 and the quarterly unaudited data for the first three quarters of 2006 and all of 2005.

b) *Changes in internal controls:* Except as described below, there were no changes in internal controls over financial reporting that occurred during the period covered by this report that have materially affected, or are reasonably likely to materially effect, our internal control over financial reporting.

#### **Changes in Internal Controls**

In addition to the remedial measures undertaken during the three months ended September 30, 2006, that we have subsequently implemented the following additional measures to address the identified material weaknesses:

- We reviewed all convertible securities to identify any securities that may have embedded beneficial conversion features or derivatives; and
- We have improved the supervision and training of our accounting staff to understand and implement applicable accounting requirements, policies and procedures applicable to the accounting and disclosure of convertible securities and derivatives.

## PART II--OTHER INFORMATION

### ITEM 1. LEGAL PROCEEDINGS

From time to time, we may become involved in various lawsuits and legal proceedings which arise in the ordinary course of business. However, litigation is subject to inherent uncertainties, and an adverse result in these or other matters may arise from time to time that may harm our business. Except as described below, we are currently not aware of any such legal proceedings that we believe will have, individually or in the aggregate, a material adverse affect on our business, financial condition or operating results.

*Paul Reep v. Applied DNA Sciences, Inc., Case No.: BC345702*

Plaintiff Paul Reep, a former employee, commenced this action against us on January 10, 2006. Mr. Reep asserted eight causes of action for breach of contract, breach of an oral agreement, negligent misrepresentation, interference with prospective business advantages, defamation, fraud, accounting and constructive trust, unjust enrichment. The relief sought included declaratory relief, unspecified compensatory damages, unpaid salary, unspecified penalties under the California Labor Code, interest, and attorneys' fees. We successfully moved the court to indefinitely stay all proceedings in this matter in light of a forum selection clause designating Nevada state courts as the proper forum. On April 11, 2007, Paul Reep filed suit against us, Applied DNA Operations Management, Inc., APDN (B.V.I.), Inc., Jun-Jei Sheu, Ben Liang, James A. Hayward, Larry Lee and Peter Brocklesby in the Clark County District Court, Nevada (Paul Reep v. Applied DNA Sciences, et al., Clark County District Court Case No. A539250). The action is a refiling of a prior lawsuit (Paul Reep v. Applied DNA Sciences, Inc., U.S. District Court, Central District of California, Case No.: BC345702). The complaint alleges causes of action for breach of written contract, breach of oral contract, defamation, fraud and violations of the California Labor Code, and seeks approximately \$360,000 in specified damages, additional damages according to proof, potential punitive damages, and fees and costs. We have not been served with the complaint or summons with respect to this matter. We dispute all of the allegations and intends to vigorously defend this action. This matter is in its early stages.

*Douglas A. Falkner v. Applied DNA Sciences, Inc./N.C. Industrial Commission File No. 585698*

Plaintiff Douglas Falkner ("Falkner") filed a worker's compensation claim in North Carolina for an alleged work-related neck injury that he alleges occurred on January 14, 2004. Falkner worked as Business Development and Operations Manager at our sole East Coast office at the time of the alleged injury. Plaintiff Falkner was the only employee employed by us in North Carolina at the time of the alleged injury and we have employed no other employees in North Carolina at any other time. The claim has been denied and is being defended on several grounds, including the lack of both personal and subject matter jurisdiction. Specifically, we contend that we did not employ the requisite minimum number of employees in North Carolina at the time of the alleged injury and that the company is therefore not subject to the North Carolina Workers' Compensation Act. The claim was originally set for hearing in January 2007, but was continued to allow the parties to engage in further discovery.

*Applied DNA Sciences, Inc. v. John Barnett, Adrian Butash, Jamie Cardona, Chanty Cheang, Paul Reep, Angela Wiggins, Peter Brocklesby, and Cheri Lu Brocklesby, Los Angeles Superior Court Case No. BC367661*

We filed this action on March 12, 2007, alleging breach of fiduciary duty and unjust enrichment against a group of our former officers and employees arising out of the unauthorized issuance of 8.25 million shares of our common stock. The suit seeks damages equal to the value of such stock on the date it was issued, or approximately \$4 million, plus other incidental damages. The case has been dismissed against defendants Barnett, Butash, Cardona, Cheang, and Wiggins as part of the previously disclosed settlement of BC350904, but proceeds against defendants Peter and Cheri Brocklesby and Paul Reep. The case is in its early stages.

*Settlement of Litigation*

On May 2, 2007, we, APDN (B.V.I.) Inc., our wholly-owned subsidiary, Applied DNA Operations Management, Inc., our wholly-owned subsidiary, James A. Hayward, our Chief Executive Officer and one of our directors, and Jun-Jei Sheu, one of our directors (the “Applied DNA parties”), entered into agreements with each of Angela Wiggins, John D. Barnett, Chanty Cheang and Adrian Butash, Jaime Cardona, all of whom are either a former employee or consultant of ours (collectively, the “former employees and consultants”) to settle certain pending litigation and all other claims arising out of the former employees’ and consultants’ employment or consulting relationships with us.

Pursuant to the terms of these settlement agreements, the Applied DNA parties on the one hand, and the former employees and consultants on the other, agreed to release each other from any and all liabilities in connection with or arising from the former employees' and consultants' prior employment or consulting relationships, and to dismiss certain lawsuits previously disclosed by us, including the following: Applied DNA Sciences, Inc. v. Paul Reep, Adrian Butash, John Barnett, Chanty Cheang, Jaime Cardona, and Angela Wiggins (U.S. District Court for the Central District of California case number CV06-2027 RGK); Barnett, et al. v. Applied DNA Sciences, et al., Los Angeles County Superior Court (case number BC 350904); Angela Wiggins v. Applied DNA Sciences, Inc., Applied DNA Operations Management, Inc., APDN (B.V.I.) Inc., Peter Brocklesby and James A. Hayward (Los Angeles Superior Court case number BC369331), which was filed by Angela Wiggins on April 10, 2007. In exchange for the consideration referenced in the Settlement Agreement, the Company agreed to pay the former employees and consultants an aggregate amount of \$605,000 in cash in five equal installments due on the first day of each month over the five month period beginning on June 1, 2007.

The settlement agreements provide that each of the former employees and consultants can cause a judgment to be entered against us, APDN (B.V.I.) Inc. and Applied DNA Operations Management, Inc. (and not the individual Applied DNA Parties) in an amount equal to three times the remaining balance due to such former employee or consultant under the applicable settlement agreement, plus interest, if we default on our payment obligation to such person and we do not satisfy it within the ten day period after receiving notice of such default.

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

None.

#### ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

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

As a company that reports under Section 15(d) of the Securities Exchange Act, we are not subject to the proxy rules of Section 14. In accordance with Nevada law and pursuant to our bylaws, we sought the approval of the matters described below through the solicitation of proxies. Our annual meeting of stockholders was held on May 16, 2007. At the meeting, the stockholders:

- (1) voted to reelect the existing members of the board of directors, James A. Hayward, Yacov Shamash, Jun-Jei Sheu and Sanford R. Simon, each for a one-year term or until their successors are duly elected and qualified;
- (2) ratified the appointment of Russell Bedford Stefanou Mirchandani LLP as the Company's independent registered public accounting firm for the fiscal year ending September 30, 2007;
- (3) approved an amendment to the Company's Articles of Incorporation to increase the number of shares of common stock the Company has the authority to issue to 410,000,000; and
- (4) approved an amendment to the Company's 2005 Incentive Stock Plan to increase the number of shares of common stock subject to the Plan to 20,000,000.

The number of votes cast for, against or withheld, and the number of abstentions with respect to each such matter is set forth below.

<b>MATTER</b>	<b>FOR</b>	<b>AGAINST/WITHHELD</b>	<b>ABSTAINED</b>
(1) Election of Directors:			
James A. Hayward	68,129,155	145,708	
Yacov Shamash	66,493,485	1,781,378	
Jun-Jei Sheu	68,129,023	145,840	
Sanford R. Simon	67,799,163	475,700	
(2) Ratification of Auditors	67,895,259	249,050	130,554
(3) Ratification and Approval of the Charter Amendment	64,915,372	3,326,883	32,607
(4) Ratification and Approval of the Charter Amendment	44,010,949	2,904,837	127,756

#### ITEM 5. OTHER INFORMATION

None.

#### ITEM 6. EXHIBITS

- 10.5 Technology Reseller Agreement, dated March 19, 2007 by and between Applied DNA Sciences and HPT International LLC, filed as an exhibit to the current report on Form 8-K filed with the SEC on March 23, 2007 and incorporated herein by reference.
- 31.1 Certification of Chief Executive Officer pursuant to Rule 13a-14 and Rule 15d-14(a), promulgated under the Securities and Exchange Act of 1934, as amended.
- 31.2 Certification of Chief Financial Officer pursuant to Rule 13a-14 and Rule 15d-14(a), promulgated under the Securities and Exchange Act of 1934, as amended.
- 32.1 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Chief Executive Officer).
- 32.2 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Chief Financial Officer).

**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.

**APPLIED DNA SCIENCES, INC.**

Date: May 21, 2007

By: /s/ JAMES A. HAYWARD  
James A. Hayward  
Chief Executive Officer (Principal Executive  
Officer, Principal Financial Officer and  
Principal Accounting Officer)