ISOLAGEN INC
Form 10-Q/A
November 12, 2003

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10 - Q/A

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

FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2003

OR

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

ISOLAGEN, INC.
(Exact name of registrant as specified in its charter)

| Delaware | 0-12666 | 87-0458888 |
|---|---|---|
| (State or other jurisdiction of incorporation) | (Commission File Number) | (I.R.S. Employer Identification No.) |

2500 Wilcrest, 5th Floor
Houston, Texas 77042
(Address of principal executive offices, including zip code)

(713) 780-4754
(Registrant's telephone number, including area code)

Check whether the issuer: (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for any 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. [X] Yes [ ] No

Check whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act.) [ ] Yes [X] No

As of May 14, 2003, issuer had 15,310,181 shares of issued and outstanding common stock, par value $0.001.

EXPLANATORY NOTE

THIS QUARTERLY REPORT ON FORM 10-Q/A IS BEING FILED FOR THE PURPOSE OF AMENDING AND RESTATING ITEMS 1 AND 2 OF PART 1 SOLELY TO THE EXTENT NECESSARY (I) TO REFLECT THE RESTATEMENT OF OUR CONSOLIDATED FINANCIAL STATEMENTS AS OF AND FOR THE THREE MONTH PERIODS ENDED MARCH 31, 2003 AND MARCH 31 2002 AS DESCRIBED IN NOTE 2 TO THE CONSOLIDATED FINANCIAL STATEMENTS, (II) TO MAKE REVISIONS TO "MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS", AS WARRANTED BY THE RESTATEMENT, (III) TO INCLUDE THE CERTIFICATIONS REQUIRED BY THE SARBANES-OXLEY ACT OF 2002 AND (IV) TO UPDATE THE EXHIBITS AND REPORTS ON FORM 8-K IN ACCORDANCE WITH THE AMENDMENT. WE HAVE MADE NO FURTHER CHANGES TO THE PREVIOUSLY FILED FORM 10-Q. ALL INFORMATION IN THIS QUARTERLY REPORT ON FORM 10-Q/A IS AS OF MARCH 31, 2003 AND DOES NOT REFLECT ANY

SUBSEQUENT INFORMATION OR EVENTS OTHER THAN THOSE REFLECTED IN THE RESTATEMENT.

Isolagen, Inc. has not amended its Annual Report on Form 10-KSB for the period ended December 31, 2001 or Quarterly Reports on Form 10-QSB for the periods affected by the restatement during the year ended December 31, 2001, therefore, the consolidated financial statements and related financial information contained therein should no longer be relied upon. The consolidated balance sheet for the year ended December 31, 2002 and the consolidated statement of operations and cash flows for the period ended March 31, 2002 are included as part of the consolidated financial statements included in this Quarterly Report on Form 10-Q/A. See Isolagen's Annual Report on Form 10-KSB/A for the period ended December 31, 2002 for more information on the effects of the restatement on prior periods.

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PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

Isolagen, Inc.
(A Development Stage Company)
Consolidated Balance Sheets

| | March 31, 2003 | December 3 2002 |
|---|---|---|
| | (unaudited) | |
| | (as restated) | (as restat |
| ASSETS | | |
| Current assets | | |
| Cash and cash equivalents | $ 1,352,584 | $ 4,244,6 |
| Accounts receivable, net of allowance for doubtful accounts | 77,381 | 40,2 |
| Inventory | 250,807 | 138,9 |
| Other receivables | 108,972 | 153,5 |
| Prepaid expenses | 277,399 | 284,5 |
| Total current assets | 2,067,143 | 4,861,8 |
| Property and equipment, net | 2,788,648 | 2,159,9 |
| Intangible assets | 540,000 | |
| Other assets | 99,085 | 235,8 |
| Total assets | $ 5,494,876 | $ 7,257,6 |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| Current liabilities | | |
| Accounts payable | $ 1,489,249 | $ 1,881,2 |
| Accrued expenses | 398,245 | 112,2 |
| Deferred revenue | 164,589 | 57,2 |
| Total current liabilities | 2,052,083 | 2,050,7 |
| Total liabilities | 2,052,083 | 2,050,7 |
| Commitments and contingencies | | |
| Shareholders' equity (deficit) | | |
| Preferred stock, $.001 par value; 5,000,000 shares authorized | 3,039 | 3,0 |
| Common stock, $.001 par value; 50,000,000 shares authorized | 15,311 | 15,2 |
| Additional paid-in capital | 26,186,857 | 25,573,9 |
| Other comprehensive income | 35,680 | 13,8 |
| Accumulated deficit during development stage | (22,798,094) | (20,399,2 |
| Total shareholders' equity (deficit) | 3,442,793 | 5,206,9 |
| Total liabilities and shareholder's equity | $ 5,494,876 | $ 7,257,6 |

The accompanying notes are an integral part of these statements. 1

Isolagen, Inc.
(A Development Stage Company)
Consolidated Statements of Operations
(unaudited)

| | Three Months Ended March 31, | | Cumulative from Decem 1995 (dat inception March |
|---|---|---|---|
| | 2003 | 2002 | 2003 |
| | (as restated) | (as restated) | (as rest |
| Revenues | | | |
| Sales | $ 371 | $ 2,518 | $ 1,441 |
| License fees | -- | 20,000 | 260 |
| Total revenues | 371 | 22,518 | 1,701 |
| Cost of sales | 994 | -- | 438 |
| Gross profit | (623) | 22,518 | 1,262 |
| Selling, general and administrative expenses | 1,660,490 | 548,512 | 8,821 |
| Research and development | 591,081 | 225,082 | 4,361 |
| Operating loss | (2,252,194) | (751,076) | (11,919 |
| Other income (expense) | | | |
| Interest income | 7,430 | 4,538 | 244 |
| Other income | 55,663 | -- | 88 |
| Loss on disposal of asset | -- | -- | (8 |
| Interest expense | -- | -- | (311 |
| Net loss | $ (2,189,101) | $ (746,538) | $(11,906 |
| Deemed dividend associated with beneficial conversion of preferred stock | $ -- | $ -- | $(10,178 |
| Preferred stock dividends | (209,782) | -- | (712 |
| Net loss attributable to common stockholders | $ (2,398,883) | $ (746,538) | $(22,798 |
| Per shares information | | | |
| Net loss - basic and diluted | $ (0.14) | $ (0.05) | $ ( |
| Deemed dividend associated with beneficial conversion of preferred stock | -- | -- | ( |
| Preferred stock dividends | (0.01) | -- | ( |
| Net loss common share - basic and diluted | $ (0.15) | $ (0.05) | $ ( |
| Weighted average number of basic and diluted common shares outstanding | 15,355,855 | 15,189,563 | 11,263 |

The accompanying notes are an integral part of these statements. 2

Isolagen, Inc.
(A Development Stage Company)
Consolidated Statements of Cash Flows

P

| | Three Months Ended March 31, | | D 19 i |
|---|---|---|---|
| | 2003 | 2002 | |
| | (as restated) | (as restated) | (a |
| Cash flows from operating activities | | | |
| Net loss | $(2,189,101) | $ (746,538) | $ |
| Adjustments to reconcile net loss to net cash used in operating activities: | | | |
| Common stock issued for services | -- | 18,031 | |
| Uncompensated contribution of services | 100,000 | 100,000 | |
| Depreciation | 143,388 | 4,069 | |
| Loss on sale of property and equipment | -- | -- | |
| Change in operating assets and liabilities: | | | |
| Increase in accounts receivable | (37,177) | (161) | |
| Increase (decrease) in other receivables | 44,611 | -- | |
| Increase in inventory | (111,897) | -- | |
| Increase (decrease) in prepaid expenses | 7,158 | -- | |
| Increase (decrease) in other assets | 17,313 | -- | |
| Increase (decrease) in accounts payable | (391,987) | 49,540 | |
| Increase in accrued expenses | 76,239 | 46,207 | |
| Increase (decrease) in deferred revenue | 107,315 | (20,000) | |
| Net cash used in operating activities | (2,234,138) | (548,852) | |
| Cash flows from investing activities | | | |
| Purchase of property and equipment | (772,123) | (4,201) | |
| Proceeds from the sale of property and equipment | -- | -- | |
| Net cash used in investing activities | (772,123) | (4,201) | |
| Cash flows from financing activities | | | |
| Proceeds from the issuance of preferred stock | -- | -- | |
| Proceeds from convertible debt | -- | -- | |
| Proceeds from notes payable to shareholders | -- | -- | |
| Proceeds from the issuance of common stock | 92,400 | -- | |
| Merger and acquisition expenses | -- | -- | |
| Repurchase of common stock | -- | -- | |
| Net cash provided by financing activities | 92,400 | -- | |
| Effect of exchange rate changes on cash balance | 21,805 | -- | |
| Net increase (decrease) in cash and cash equivalents | (2,892,056) | (553,053) | |
| Cash and cash equivalents, beginning of period | 4,244,640 | 1,380,824 | |
| Cash and cash equivalents, end of period | $ 1,352,584 | $ 827,771 | $ |
| Supplemental cash flow information: | | | |
| Cash paid for interest | $ -- | $ -- | $ |
| Deemed dividend associated with beneficial conversion of preferred stock | -- | -- | |
| Preferred stock dividend | 209,782 | -- | |
| Common stock issued for services | -- | 18,031 | |
| Uncompensated contribution of services | 100,000 | 100,000 | |

The accompanying notes are an integral part of these statements. 3

Isolagen, Inc.
(A Development Stage Company)
Notes to Unaudited Consolidated Financial Statements

NOTE 1 - BASIS OF PRESENTATION, BUSINESS AND ORGANIZATION

Isolagen, Inc. f/k/a American Financial Holding, Inc., a Delaware corporation ("Isolagen" or the "Company") is the parent company of Isolagen Technologies, Inc., a Delaware corporation ("Isolagen Technologies"). Isolagen Technologies is the parent company of Isolagen Europe Limited, a company organized under the laws of the United Kingdom and wholly-owned subsidiary of Isolagen Technologies ("Isolagen Europe"). Isolagen Technologies is the parent company of Isolagen Australia Pty Limited, a company organized under the laws of the Australia and wholly-owned subsidiary of Isolagen Technologies ("Isolagen Australia"). The common stock, par value $0.001 per share, of the Company ("Common Stock") is traded on the American Stock Exchange ("AMEX") under the symbol "ILE."

Isolagen is a Houston, Texas based specialty pharmaceutical bioscience company which has developed a patented process for the propagation of autologous cells to be used to stimulate a patient's own collagen and elastin production (the "Isolagen Process"). Autologous cells are a patient's own cells taken from a small skin sample. From such sample millions of cells are grown and then injected into the patient to correct and reduce the normal effects of aging like wrinkles, laugh lines, smokers lines, fine lines and all types of depressed scars. The procedure is minimally invasive and non-surgical.

In 1995, Isolagen Technologies began treating a small percentage of patients with the Isolagen Process to correct defects (e.g., wrinkles, depressions and scarring) in the patient's face. Between 1995 and 1999, approximately 200 doctors utilized the Isolagen Process on approximately 963 patients with positive results. In 1997, the FDA began regulating the science of biologics. Biologics, in contrast to drugs that are chemically synthesized, are derived from living sources (such as humans, animals, and microorganisms) like the Isolagen Process. In 1995, when Isolagen Technologies began operations, the FDA had no regulations governing this area of biologics. After reviewing the new regulations and seeking the advice of consultants, Isolagen concluded that the use of the Isolagen Process in cosmetic applications did not require the approval of the FDA. In 1999, Isolagen Technologies filed a request for authorization from the FDA to administer an investigational drug or biological product to humans (referred to herein as an "IND"). Such authorization must be secured prior to commercialization of any new drug or biological product. The FDA placed the IND on clinical hold until Isolagen Technologies' manufacturing processes and procedures were changed to meet these new biologics standards, and FDA approval is obtained. In April 2002, the FDA released Isolagen's IND and clinical trial negotiations are underway.

As a result, a 397 patient retrospective study has been completed. The results demonstrated both safety and efficacy as Phase II data. Using Isolagen Technologies recently completed cGMP laboratory facility in Houston, Texas, several studies are taking place. These include: dosage management, dental application relating to gum and bone, cosmetic correction and scarring. They are operational under currently active INDs with the FDA. The Company anticipates that these INDs are scheduled for License Application (approval) by the FDA in 2003, although there can be no assurance that such approval will be obtained or obtained on a timely basis.

The Company's goal is to become the industry leader in the research, development and commercialization of the Isolagen Process and the use of autologous cellular systems ("ACS") which stimulate a patient's own collagen production. The Company is also pursuing, through Isolagen Europe, commercial operations in the United Kingdom and is pursuing commercial operations through subsidiaries, joint ventures or license arrangements in Australia, South Korea, Hong Kong, Brazil, Mexico and elsewhere. The Company is investigating regulatory and other requirements in these countries and evaluating markets and potential joint venture partners and licensees.

Through March 31 2003, the Company has been primarily engaged in developing its initial product technology, recruiting personnel, commencing its United Kingdom operations and raising capital. In the course of its development activities, the Company has sustained losses and expects such losses to continue through at least the balance of 2003. The Company will finance its operations primarily through its existing cash, future financing and revenues.



The Company's ability to operate profitably under its current business plan is largely contingent upon its success in obtaining further sources of debt and equity capital, prompt regulatory approval to sell its products and upon its continued expansion. The Company will require additional capital in the future to expand its operations. No assurance can be given that the Company will be able to obtain any such additional capital, either through equity or debt financing, on satisfactory terms or at all. Additionally, no assurance can be given that any such financing, if obtained, will be adequate to meet the Company's ultimate capital needs and to support the Company's growth. If adequate capital cannot be obtained on satisfactory terms, the Company's operations could be negatively impacted.

If the Company achieves growth in its operations in the next few years, such growth could place a strain on its management, administrative, operational and financial infrastructure. The Company's ability to manage its operations and growth requires the continued improvement of operational, financial and management controls, reporting systems and procedures. In addition, the Company may find it necessary to hire additional management, financial and sales and marketing personnel to manage the Company's expanding operations. If the Company is unable to manage this growth effectively and successfully, the Company's business, operating results and financial condition may be materially adversely affected.

As of March 31, 2003, the Company had a cash balance of $1,352,584. As of May 5, 2003, the Company had a cash balance of approximately $0.6 million. The Company does not have any credit facilities with which to fund ongoing working capital needs. On May 9, 2003, the Company sold 110,250 shares of Series B Convertible Preferred Stock for a gross amount of approximately $3.1 million. After deducting the costs and expenses associated with the sale, the Company received approximately $2.8 million. The long-term viability of the Company is dependent upon successful operation of its business and the ability to raise additional debt and equity within the near future.

Acquisition and merger and basis of presentation

On August 10, 2001, Isolagen Technologies consummated a merger with American Financial Holdings, Inc. ("AFH") and Gemini IX, Inc. ("Gemini"). Pursuant to an Agreement and Plan of Merger, dated August 1, 2001, by and among AFH, ISO Acquisition Corp, a Delaware corporation and wholly-owned subsidiary of AFH ("Merger Sub"), Isolagen Technologies, Gemini, a Delaware corporation, and William J Boss, Jr., Olga Marko and Dennis McGill, stockholders of Isolagen

Technologies (the "Merger Agreement"), AFH (i) issued 5,453,977 shares of its common stock, par value $0.001 to acquire, in a privately negotiated transaction, 100% of the issued and outstanding common stock (195,707 shares, par value $0.01, including the shares issued immediately prior to the Merger for the conversion of certain liabilities, as discussed below) of Isolagen Technologies, and (ii) issued 3,942,000 shares of its common stock to acquire 100% of the issued and outstanding common stock of Gemini. Pursuant to the terms of the Merger Agreement, Merger Sub, together with Gemini, merged with and into Isolagen Technologies (the "Merger"), and AFH was the surviving corporation. AFH subsequently changed its name to Isolagen, Inc. on November 13, 2001.

Prior to the Merger, Isolagen Technologies had no active business and was seeking funding to begin U.S. Food and Drug Administration ("FDA") trials of the Isolagen Process. AFH was a non-operating, public shell company with limited assets. Gemini was a non-operating private company with limited assets and was unaffiliated with AFH.

Since AFH and Gemini had no operations and limited assets at the time of the Merger, the merger has been accounted for as a recapitalization of Isolagen Technologies and an issuance of common stock by Isolagen Technologies for the net assets of AFH and Gemini. In the recapitalization, Isolagen Technologies is treated as having affected (i) a 27.8694 for 1 stock split, whereby the 195,707 shares of its common stock outstanding immediately prior the merger are converted into the 5,453,977 shares of common stock received and held by the Isolagen Technologies stockholders immediately after the merger, and (ii) a change in the par value of its common stock, from $0.01 per share to $0.001 per share. The stock split has been reflected in the accompanying consolidated financial statements by retroactively restating all shares and per share amounts. The change in par value is reflected by a transfer between the common stock and additional paid-in capital accounts at the date of the Merger. The stock issuances are accounted for as the issuance of (i) 3,942,400 shares for the net assets of Gemini, recorded at their book value, and (ii) the issuance of 3,899,547 shares (the number of shares AFH had outstanding immediately prior to the Merger) for the net assets of AFH, recorded at their book value.



Immediately prior to and as a condition of the Merger, Isolagen Technologies issued an aggregate of 2,328,972 shares (post split) of its common stock to convert to equity an aggregate of $2,075,246 of liabilities, comprised of (i) accrued salaries of $328,125, (ii) convertible debt and related accrued interest of $1,611,346, (iii) convertible shareholder notes and related accrued interest of $135,667 and (iv) bridge financing costs of $108. Simultaneous with the Merger, the Company sold 1,346,669 shares of restricted common stock to certain accredited investors in a private placement transaction. The consideration paid by such investors for the shares of common stock aggregated $2,020,000 in transactions exempt from the registration requirements of the Securities Act. The net cash proceeds of this private placement were used to fund Isolagen's research and development projects and the initial FDA trials of the Isolagen Process, to explore the viability of entering foreign markets, to provide working capital and for general corporate purposes.

The financial statements presented include Isolagen, Inc. and its wholly-owned subsidiaries. All significant intercompany transactions and balances have been eliminated. Isolagen Technologies was, for accounting purposes, the continuing entity of the Merger, and accordingly for the periods prior to the Merger, the financial statements reflect the financial position, results of operations and cash flows of Isolagen Technologies. The assets, liabilities, operations and cash flows of AFH and Gemini are included in the consolidated financial statements from August 10, 2001 onward.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Interim financial information

The financial statements included herein, which have not been audited pursuant to the rules and regulations of the Securities and Exchange Commission, reflect all adjustments which, in the opinion of management, are necessary for a fair presentation of financial position, results of operations and cash flows for the interim periods on a basis consistent with the annual audited statements. All such adjustments are of a normal recurring nature. The results of operations for interim periods are not necessarily indicative of the results that may be expected for any other interim period of a full year. Certain information, accounting policies and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been omitted pursuant to such rules and regulation, although the Company believes that the disclosures are adequate to make the information presented not misleading, These financial statements should be read in conjunction with the Company's audited financial statements included in the Company's current report on Form 10-KSB filed with the Securities and Exchange Commission on March 31, 2003.

Restatement of financial statements

Subsequent to the issuance of the Company's financial statements as of March 31, 2003 and for the three month periods ended March 31, 2003 and 2002, the Company identified several errors that were required to be corrected in the previously reported financial statements. The principal reasons and effects of the adjustments are summarized below:

Beneficial Conversion Feature: During 2002, the Company completed private placements of Series A Convertible Preferred Stock. Imbedded within the instruments was a beneficial conversion feature that was not recorded. Accordingly, the Company revised its financial statements as of March 31, 2003 and for the three month periods ended March 31, 2003 and 2002 to record deemed dividends to the holders of the preferred stock totaling $0 and $0 for the three month periods ended March 31, 2003 and 2002, respectively. The Company's financial statements reflect an increase in the retained deficit and a corresponding increase in paid-in capital for this amount. The deemed dividend associated with the beneficial conversion is calculated as the difference between the fair value of the underlying common stock less the proceeds that have been received for the Series A Preferred Stock limited to the value of the proceeds received. Also, the Company has included preferred dividends accrued for the three months ended March 31, 2003 and 2002 of $209,782 and $0, respectively, in the computation of net loss attributable to common shareholders.

Contributed Services: During 2003, 2002 and 2001, certain officers and directors of the Company were not compensated for a portion of their services provided to Company. The financial statements are to reflect the total



cost of conducting its business which includes the value of contributed services. Accordingly, the Company has recorded contribution services from officers totaling $100,000 for each of the three month periods ended March 31, 2003 and 2002, respectively. We estimated the value of the contributed services based upon our estimate of their fair market value. This contribution of services was recorded as an increase in compensation expense and an increase in additional paid in capital.

Weighted Average Shares Utilized in the Calculation Percentage Loss Per

Share: Similar to a reverse merger, the weighted average shares outstanding utilized in the computation of earnings per share are to be adjusted to give effect as if the Merger transaction had occurred as of the beginning of the earliest year presented, similar to a stock split. For all years presented prior to the Merger, the weighted average shares outstanding were not adjusted to reflect the recapitalization as of the earliest period presented. Accordingly, the Company has retroactively restated its financial statements to the earliest period presented for the purposes of computing weighted average shares outstanding and loss per share data.

Together these restatements changed the net loss per share attributable to common shareholders from $0.14 to $0.15 for the three months ended March 31, 2003, from $0.04 to $0.05 for the three months ended March 31, 2002, and the cumulative from inception net loss per share has decreased from $2.08 to $2.02.

Statement of cash flows

For purposes of the statements of cash flows, the Company considers all highly liquid debt instruments purchased with an original maturity of three months or less to be cash equivalents.

Concentration of credit risk

The Company maintains its cash with a major U.S. domestic bank. The amounts held in this bank exceed the insured limit of $100,000 from time to time. The terms of these deposits are on demand to minimize risk. The Company has not incurred losses related to these deposits.

The Company is subject to risks common to companies in the development stage including, but not limited to, development of new products, development of markets and distribution channels, dependence on key personnel, and the ability to obtain additional capital as needed to fund its product plans. The Company has a limited operating history and has yet to generate any significant revenues from customers. To date, the Company has been funded by private debt and equity financings. The Company's ultimate success is dependent upon its ability to raise additional capital and to successfully develop and market its products.

The products developed by the Company require approvals from the United States FDA or other international regulatory agencies prior to commercial sales. There can be no assurance that all of the Company's products will receive the necessary approvals. If the Company was denied such approvals or such approvals were delayed, it may have a material adverse impact on the Company.

Inventory

Inventory primarily consists of raw materials used in the Isolagen Process. Inventory is stated at the lower of cost or market and cost is determined by the weighted average method.

Property and equipment

Property and equipment, consisting primarily of lab equipment, computer equipment, leasehold improvements, and office furniture and fixtures is carried at cost less accumulated depreciation. Depreciation for financial reporting purposes is provided by the straight-line method over the estimated useful lives of three to five years subject to half year convention. Leasehold improvements are amortized using the straight-line method over the remaining life of the lease. The cost of repairs and maintenance is charged against income as incurred.

Intangible assets

In the first quarter of 2003, the Company entered into an Intellectual Property Purchase Agreement to acquire two pending patent applications. As consideration, the Company issued the seller 100,000 shares of its Common Stock and royalty equal to (a) 5% of all revenues recognized by the Company or its Affiliates from commercial application of the Intellectual Property made, provided, distributed, sold or manufactured directly by the Company or its Affiliates, or (b) 25% of all revenues recognized by the Company or its Affiliates from licensing, sublicensing, transferring or selling the Intellectual Property to a third party, without offset or deduction for general and administrative or operating costs, subject to a total maximum royalty of $2 million. The pending patent applications are recorded as intangible assets at their acquisition cost and will be amortized over their estimated useful lives on a straight-line basis.

Earnings per share data

Basic earnings (loss) per share is calculated based on the weighted average common shares outstanding during the period. Diluted earnings per share also gives effect to the dilutive effect of stock options, warrants and convertible preferred stock (calculated based on the treasury stock method). The Company does not present diluted earnings per share for years in which it incurred net losses as the effect is antidilutive.

Shares of Isolagen common stock outstanding prior to the Merger were deemed converted to its equivalent shares of the Company's common stock using a conversion factor as defined in the Merger Agreement.

Stock-based compensation

The Company accounts for its stock-based compensation under the provisions of Statement of Financial Accounting Standards ("SFAS") No. 123 - "Accounting for Stock Based Compensation." Under SFAS No. 123, the Company is permitted to either record expenses for stock options and other employee compensation plans based on their fair value at the date of grant or to continue to apply its current accounting policy under Accounting Principles Board Opinion No. 25 "Accounting for Stock Issued to Employees," ("APB No. 25"), and recognize compensation expense, if any, based on the intrinsic value of the equity instrument at the measurement date. The Company elected to continue following the provisions of APB No. 25.

In December 2002, the Financial Accounting Standards Board ("FASB") issued SFAS No. 148, "Accounting for Stock-Based Compensation-Transition and Disclosure". This statement provides guidance for those companies wishing to voluntarily change to the fair value based method of accounting for stock-based compensation. The statement also amends the disclosure requirements of SFAS No, 123, requiring prominent disclosure in annual and interim financial statements regarding a company's method for accounting for stock-based employee compensation and the effect of the method on reported results. While Isolagen continues to utilize the disclosure-only provisions of SFAS No. 123, it has modified its disclosures to comply with the new statement.

Income taxes

An asset and liability approach is used for financial accounting and reporting for income taxes. Deferred income taxes arise from temporary differences between income tax and financial reporting and principally relate to recognition of revenue and expenses in different periods for financial and tax accounting purposes and are measured using currently enacted tax rates and laws. In addition, a deferred tax asset can be generated by net operating loss

carryforwards ("NOLs"). If it is more likely than not that some portion or all of a deferred tax asset will not be realized, a valuation allowance is recognized.

Revenue recognition

The Company recognizes revenue from product sales when goods are shipped and the risk of loss transfers to the customer. Revenue from licenses and other upfront fees are recognized on a ratable basis over the term of the respective agreement. Milestone payments are recognized upon successful completion of a performance milestone event. Any amounts received in advance of performance are recorded as deferred revenue. The Company recognizes revenue over the period the service is performed in accordance with SEC Staff Accounting Bulletin No. 101,



"Revenue Recognition in Financial Statements" ("SAB 101"). 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 or services rendered, (3) the fee is fixed and determinable, and (4) collectibility is reasonably assured. We believe that all of these conditions are met at the time of shipment. Currently, three injections are recommended, although the decision to utilize one, two or three injections is between the attending physician and his/her patient. The amount invoiced is fixed and determinable and only varies among customers depending upon the number of injections requested. There is no performance provision under any arrangement with any doctor and there is no right to refund, or returns for unused injections.

Currently the Isolagen Process is delivered through an attending physician to each patient in the Company's recommended regimen of up to three injections. Each injection has stand alone value to the patient. The Company invoices the attending physician upon that physician submitting his/her patient's tissue sample to the Company; thus the contractual arrangement is between the Company and the medical professional. The amount invoiced varies directly with the number of injections requested. All orders are paid in advance by the physician and are not refundable. Revenue is deferred until shipment, provided no significant obligations remain, and is recognized in installments corresponding to the number of injections shipped to the attending physician. Due to the short shelf life, each injection is cultured on an as needed basis and shipped prior to the individual injection being administered by the physician. The amount of the revenue deferral represents the fair value of the remaining undelivered injections defined in accordance with EITF 00-21, which addresses the issue of accounting for arrangements that involve the delivery of multiple products or services. Should the physician discontinue the regimen prematurely all remaining deferred revenue is recognized.

Promotional incentives

The Company periodically offers promotional incentives to physicians on a case-by-case basis. Promotional incentives are provided to physicians in the form of 'at no charge' Isolagen Treatments and Isolagen Treatments offered at a discount to the suggested price list. The Company does not receive any identifiable benefit from the physicians in exchange for any promotional incentives granted.

The Company does not record any revenue related to 'at no charge' Isolagen Treatments and the cost to provide such treatments is expensed as incurred. The Company records any discounts granted as a reduction in revenue (i.e.net revenue after discount) from that specific transaction. The Company believes this accounting treatment complies with Emerging Issues Task Force ("EITF")-01-09: Accounting for Consideration Given by a Vendor to a Customer (Including a

Reseller of the Vendor's Products).

Foreign currency translation

The financial position and results of operations of the Company's foreign subsidiaries are generally determined using the local currency as the functional currency. Assets and liabilities of these subsidiaries are translated at the exchange rate in effect at each year-end. Income statement accounts are translated at the average rate of exchange prevailing during the year. Adjustments arising from the use of differing exchange rates from period to period are included in other comprehensive income in stockholders' equity. Gains and losses resulting from foreign currency transactions are included in earnings and have not been material in any one year.

Comprehensive income

Comprehensive income encompasses all changes in equity other than those with stockholders and consists of net earnings and foreign currency translation adjustments. The Company does not provide for U.S. income taxes on foreign currency translation adjustments since it does not provide for such taxes on undistributed earnings of foreign subsidiaries.

Research and development expenses

Research and development expenses include direct costs, research-related overhead, and costs associated with improved process science, manufacturing and cost reduction are charged to operations as incurred.



Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Recent accounting pronouncements

In December 2002, the Emerging Issues Task Force, ("EITF"), issued EITF Issue 00-21, Accounting for Revenue Arrangements with Multiple Deliverables. EITF 00-21 provides guidance on determining whether a revenue arrangement contains multiple deliverable items and if so, requires that revenue be allocated amongst the different items based on fair value. EITF 00-21 also requires that revenue or any item in a revenue arrangement with multiple deliverables not delivered completely must be deferred until delivery of the item is completed. The guidance in EITF 00-21 is effective for revenue arrangements entered into in fiscal periods beginning after June 15, 2003. The Company does not expect that implementation of EITF 00-21 will have a material impact on its results of operations or financial position.

In December 2002, the FASB issued SFAS No. 148, "Accounting for Stock-Based Compensation-Transition and Disclosure". This statement provides guidance for those companies wishing to voluntarily change to the fair value based method of accounting for stock-based compensation. The statement also amends the disclosure requirements of Statement 123, requiring prominent disclosure in annual and interim financial statements regarding a company's method for accounting for stock-based employee compensation and the effect of

the method on reported results. While Isolagen continues to utilize the disclosure-only provisions of SFAS No. 123, it has modified its disclosures to comply with the new statement.

NOTE 3 - CONTINGENCIES

On October 9, 1996, the Company was advised by the Enforcement Division of the Securities and Exchange Commission (the "Commission") that it is considering recommending that the Commission bring an enforcement action, which could include a civil penalty, against the Company in U.S. District Court for failing to file timely periodic reports in violation of Section 13(a) of the Securities and Exchange Act of 1934 and the rules thereunder.

In October 1996, the Company also received a request for the voluntary production of information to the Enforcement Division of the Commission related to the resignation of Coopers & Lybrand LLP and the termination of Arthur Andersen LLP and the appointment of Jones, Jensen & Company as the Company's independent public accountants and the reasons therefore. In addition, the Company was requested to provide certain information respecting its previous sales of securities. The Company cooperated in providing information in response to these inquiries in early 1997. The Company has not been advised of the outcome of the foregoing, and has had no further contact by the Enforcement Division of the Commission.

NOTE 4 - EQUITY

From the date of the Merger through March 31, 2003, the Company has not paid compensation to certain officers and directors. Accordingly, the Company has capitalized the estimated fair value of these services. The uncompensated contributed services totaled $100,000 for each of the three month periods ended March 31, 2002 and 2003. We estimated the value of the contributed services based upon our estimate of their fair market value. This contribution of services was recorded as an increase to compensation expense and increase in additional paid in capital.

During the three months ended March 31, 2003, the Company issued 61,600 shares of common stock for cash totaling $92,400 in connection with the exercise of stock options.

During the three months ended March 31, 2003, the Company issued 1,565,000 options to purchase its common stock with exercise prices ranging from $4.50 to $6.00 per share under the 2001 and 2003 Stock Options



Plans ("Stock Option Plans"). The options vest over a three year period from the date of grant. The weighted average fair value of the options grant, based on the Black-Sholes valuation model, is estimated to be $3.58 per option. Had compensation costs for all options issued under the Stock Option Plans been determined based on the fair value at the grant date consistent with the provisions of SFAS No. 123, net income and net income per share would have decreased to the pro forma amounts indicated below:

| | Three Months Ended March 31, | |
|---|---|---|
| | 2003 | 2002 |
| Net loss - as reported | $(2,189,101) | $ (746,538) |

| | | |
|---|---|---|
| Less: total stock-based employee compensation expense determined under fair value based method for all awards granted to employees, net of related tax effect | (373,817) | (191,134) |
| Net loss - pro forma | $(2,562,918) | $ (937,673) |
| Net loss per share - as reported | | |
| Basic and diluted | $ (0.14) | $ (0.05) |
| Net loss per share - pro forma | | |
| Basic and diluted | $ (0.17) | $ (0.06) |

NOTE 5 - SUBSEQUENT EVENTS

Additional financing

On May 9, 2003, the Company sold 110,250 shares of Series B Convertible Preferred Stock for a gross amount of approximately $3.1 million. After deducting the costs and expenses associated with the sale, the Company received approximately $2.8 million.

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

The following discussions of Isolagen`s results of operations and financial position should be read in conjunction with the financial statements and notes pertaining to them that appear elsewhere in this Form 10-Q.

Certain statements contained herein are not based on historical facts, but are forward-looking statements that are based upon numerous assumptions about future conditions that could prove not to be accurate. Actual events, transactions and results may materially differ from the anticipated events, transactions or results described in such statements. The Company's ability to consummate such transactions and achieve such events or results is subject to numerous risks and uncertainties. Such risks and uncertainties include, but are not limited to, the existence of demand for and acceptance of the Company's products and services, regulatory approvals and developments, economic conditions, the impact of competition and pricing, results of financing efforts and other factors affecting the Company's business that are beyond the Company's control. The Company undertakes no obligation and does not intend to update, revise, or otherwise publicly release the results of any revisions to these forward-looking statements that may be made to reflect future events or circumstances.

Although we believe that our expectations are based on reasonable assumptions, we can give no assurance that our expectations will materialize. Many factors could cause actual results to differ materially from our forward looking statements. Several of these factors include, without limitation:

- our ability to develop autologous cellular therapies that have specific applications in cosmetic dermatology, and our ability to explore (and possibly develop) applications for periodontal disease, reconstructive dentistry and other health-related markets;

- whether our clinical human trials relating to autologous cellular therapy applications for the treatment of dermal defects or gingival recession can be conducted within the timeframe that we expect, whether

such trials will yield positive results, or whether additional applications for the commercialization of autologous cellular therapy can be identified by us and advanced into human clinical trials;

- our ability to provide and deliver any autologous cellular therapies that we may develop, on a basis is that is cost competitive with other therapies, drugs and treatments that may be provided by our competitors;

- our ability to finance our business;

- our ability to maintain our current pricing model;

- our ability to decrease our cost of goods sold;

- a stable interest rate market in the world, and specifically the countries we are doing business in or plan to do business in;

- management's best estimate on the patient data including patients started and patients completed;

- a stable currency rate environment in the world, and specifically the countries we are doing business in or plan to do business in;

- our ability to receive requisite regulatory approvals in the United States, European Community, Australia, South Korea, Hong Kong, Mexico, and our ability to retain the licenses that we have obtained and may obtain; and the absence of adverse regulatory developments in the United States, European Community, Australia, South Korea, Hong Kong, Mexico or any other country we plan to do conduct commercial operations;

- continued availability of supplies at the current prices;

- no new entrance of competitive products in our markets;

- no adverse publicity related to our products or the Company itself;

- no adverse claims relating to our Intellectual Property;

- the adoption of new, or changes in, accounting principles; and/or legal proceedings;

- our ability to maintain compliance with the AMEX requirements for continued listing of our common stock;

- the costs inherent with complying with new statutes and regulations applicable to public reporting companies, such as the Sarbanes-Oxley Act of 2002;

- our ability to efficiently integrate future acquisitions, if any;

- other new lines of business that the Company may enter in the future; and

- other risks referenced from time to time elsewhere in this report and in our filings with the SEC.

These factors are not necessarily all of the important factors that could cause actual results of operations to differ materially from those expressed in these forward-looking statements. Other unknown or unpredictable factors also could have material adverse effects on our future results. We undertake no obligation and do not intend to update, revise or otherwise publicly release any revisions to these forward-looking statements to reflect events or circumstances after the date hereof or to reflect the occurrence of any unanticipated events. We cannot assure you that projected results will be achieved.

GENERAL

Isolagen is a Houston, Texas based specialty pharmaceutical bioscience company which has developed a patented process for the propagation of autologous cells to be used to stimulate a patient's own collagen and elastin production. Autologous cells are a patient's own cells taken from a small skin sample. From such sample millions of cells can be grown and then injected into the patient to correct and reduce the normal effects of aging like wrinkles, laugh lines, smokers lines, fine lines and all types of depressed scars. The procedure is minimally invasive and non-surgical. Currently, there are multiple competitive alternatives to reduce the signs of aging, but they offer short term and often painful solutions. Their solutions often involve substitute products or fillers, such as human cadaver or animal collagen or synthetic chemicals. A well known example is Botox, which uses diluted, liquid toxin to attain a correction through muscle paralysis.

In contrast, the Isolagen Process (as described in more detail below) is a self healing protein repair system that uses only the patient's own (autologous) cells. Since these cells belong only to the patient and house his or her own DNA, there is a reduced chance for rejection or allergic reaction. It is important to note that the cells are grown individually. There is no batch manufacturing and the Company's Laboratory Information Management System keeps the cells self contained and separate.



The Isolagen Process is designed to replenish deficiencies caused through the loss of fibroblast cells as the body ages. The body losses approximately 1% of the body's fibroblast cells per year. The fibroblast cell is the cell responsible for producing collagen, "the structural matrix", that supports the skin and also produces elastin. By the time a person is 40 years old, their body has depleted approximately 40% of its fibroblast cells, thus causing dermal depressions and wrinkles. The Isolagen Process reduces dermal depressions and wrinkles by replenishing the area of deficiency with millions of the patient's own new living fibroblast cells. Within weeks after the injection, the millions of new fibroblast cells will produce new collagen and elastin and will help diminish wrinkles.

While there can be no assurance, the Company forecasts that it will begin serving a total of approximately 6,400 patients in 2003, 44,800 patients in 2004, and 157,500 patients in 2005. The Company's forecasts are based upon assumptions that the Company will have adequate capital to fund the expanded operations, and the Company will be authorized to market its products in United Kingdom, Australia, and South Korea in 2003 and the United States, Italy, Mexico, Brazil, France and Germany in 2004.

CRITICAL ACCOUNTING POLICIES

The following discussion and analysis of financial condition and results of operations are based upon the Company's consolidated financial statements, which have been prepared in conformity with accounting principles generally accepted in the United States. The preparation of these financial statements requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues, expenses and related disclosures. On an on-going basis, the Company evaluates its estimates and assumptions, including but not limited to those related to the impairment of long-lived assets, reserves for doubtful accounts, revenue recognition and certain accrued liabilities. The Company bases its estimates on historical experience and various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

Revenue Recognition: The Company recognizes revenue from product sales when goods are shipped and the risk of loss transfers to the customer. Revenue from licenses and other upfront fees are recognized on a ratable basis over the term of the respective agreement. Milestone payments are recognized upon successful completion of a performance milestone event. Any amounts received in advance of performance are recorded as deferred revenue. The Company recognizes revenue over the period the service is performed in accordance with SEC Staff Accounting Bulletin No. 101, "Revenue Recognition in Financial Statements" ("SAB 101"). 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 or services rendered, (3) the fee is fixed and determinable, and (4) collectibility is reasonably assured. We believe that all of these conditions are met at the time of shipment. Currently, three injections are recommended, although the decision to utilize one, two or three injections is between the attending physician and his/her patient. The amount invoiced is fixed and determinable and only varies among customers depending upon the number of injections requested. There is no performance provision under any arrangement with any doctor and there is no right to refund, or returns for unused injections.

Currently the Isolagen Process is delivered through an attending physician to each patient in the Company's recommended regimen of up to three injections. Each injection has stand alone value to the patient. The Company invoices the attending physician upon that physician submitting his/her patient's tissue sample to the Company; thus the contractual arrangement is between the Company and the medical professional. The amount invoiced varies directly with the number of injections requested. All orders are paid in advance by the physician and are not refundable. Revenue is deferred until shipment, provided no significant obligations remain, and is recognized in installments corresponding to the number of injections shipped to the attending physician. Due to the short shelf life, each injection is cultured on an as needed basis and shipped prior to the individual injection being administered by the physician. The amount of the revenue deferral represents the fair value of the remaining undelivered injections defined in accordance with Emerging Issues Task Force ("EITF") 00-21, which addresses the issue of accounting for arrangements that involve the delivery of multiple products or services. Should the physician discontinue the regimen prematurely all remaining deferred revenue is recognized.



Research and development expenses: Research and development expenses include direct costs, research-related overhead, and costs associated with improved process science, manufacturing and cost reduction are charged to operations as incurred.

Stock-based compensation: The Company accounts for its stock-based compensation under the provisions of SFAS No. 123 - "Accounting for Stock Based Compensation." Under SFAS No. 123, the Company is permitted to either record expenses for stock options and other employee compensation plans based on their fair value at the date of grant or to continue to apply its current accounting policy under Accounting Principles Board Opinion No. 25 "Accounting for Stock Issued to Employees," ("APB NO. 25"), and recognize compensation expense, if any, based on the intrinsic value of the equity instrument at the measurement date. The Company elected to continue following the provisions of APB No. 25.

In December 2002, the FASB issued SFAS No. 148, "Accounting for Stock-Based Compensation-Transition and Disclosure." This statement provides guidance for those companies wishing to voluntarily change to the fair value based method of accounting for stock-based compensation. The statement also amends the disclosure requirements of SFAS No. 123, requiring prominent disclosure in annual and interim financial statements regarding a company's method for accounting for stock-based employee compensation and the effect of the method on reported results. While Isolagen continues to utilize the disclosure-only provisions of SFAS No. 123, it has modified its disclosures to comply with the new statement.

RESULTS OF OPERATIONS, AS RESTATED

Comparison of the three months ending March 31, 2003 and 2002

REVENUES. Revenues decreased $22,147, to $371 for the three months ended March 31, 2003 compared to $22,518 for the three months ended March 31, 2002. The decrease in revenues is primarily attributable to $20,000 in license fees recognized in the three months ended March 31, 2002 which did not recur in the three months ended March 31, 2003.

While the Company commenced partial operations in the United Kingdom during the first three months of 2003, the Company does not expect to begin to recognize revenues from such operations until the second quarter of 2003 because of the method in which the Company recognizes its revenues. In particular, the Isolagen Process involves a patient's doctor obtaining a 3 mm punch skin sample from the patient. The skin sample is packed in a container provided by the Company and shipped overnight to the Company's laboratory. The specimen is then cultured utilizing the Company's patented Isolagen Process. This process separates the cell, called a fibroblast, from the rest of the tissue then multiplies these fibroblasts. Approximately six (6) weeks later, 1 ml is returned to the patient's doctor for an intradermal test in the patient. Two (2) weeks later, 1 to 1.5 ml of the patient's cells are also sent to the doctor for treatment. Additional amounts of 1 to 1.5 ml are available for re-injection every two (2) to three (3) weeks. The Company recognizes one-third of the revenue associated with each treatment upon the shipment of the first injection to the patient's doctor, an additional one-third of revenue associated with each treatment is recognized upon shipment of the second injection to the patient's doctor, and the remaining one-third is recognized upon the shipment of the last injection to the patient's doctor.

In addition, those revenues which the Company did recognize during the first three months of 2003 from its United Kingdom operations were in part reduced by promotional incentives provided by the Company to doctors utilizing the Isolagen Process. The Company expects to continue providing such promotional incentives to doctor's during the introduction phase of the Isolagen Process in the United Kingdom.

COST OF SALES. Costs of sales increased to $994 for the three months ended March 31, 2003 compared to $0 for the three months ended March 31, 2002. The increase in cost of sales is primarily related to the commencement of

operations in the United Kingdom.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES. Selling, general and administrative expenses increased 203%, or $1,111,978, to $1,660,490 for the three months ended March 31, 2003 compared to $548,512 for the three months ended March 31, 2002. The major components of the approximately $1.1 million increase in selling, general and administrative expense are as follows: a) consulting expense increased by



approximately $0.2 million to $0.3 million for the three months ended March 31, 2003 compared to $0.1 million for the three months ended March 31, 2002; b) salaries increased by approximately $0.1 million to $0.2 million for the three months ended March 31, 2003 compared to $0.1 million for the three months ended March 31, 2002 (these amounts include an imputed expense of $100,000 in each period relating to the fair market value of services provided by certain officers for which they will not be compensated); c) travel expense increased by approximately $0.2 million to $0.3 million for the three months ended March 31, 2003 compared to $0.1 million for the three months ended March 31, 2002; d) legal expense increased by approximately $0.1 million to $0.2 million for the three months ended March 31, 2003 compared to $0.1 million for the three months ended March 31, 2002; e) promotional expense increased by approximately $0.1 million to $0.1 million for the three months ended March 31, 2003 compared to $0.0 million for the three months ended March 31, 2002; and f) depreciation and amortization increased by approximately $0.1 million to $0.1 million for the three months ended March 31, 2003 compared to $0.0 million for the three months ended March 31, 2002. The increase in selling, general and administrative expenses is attributed primarily to: a) higher salaries expense due to an increase in the number of employees; b) increased travel expenses related to our expansion into the United Kingdom and Australia; c) higher legal fees related to patent and business development issues; d) increased marketing and promotion efforts related to the commencement of operations in the United Kingdom; and e) depreciation and amortization of assets placed into service during 2003 with the commencement of operations in the United Kingdom and the completion of the U.S laboratory.

RESEARCH AND DEVELOPMENT. Research and development expenses increased by approximately $0.4 million during the three months ended March 31 2003 to $0.6 million as compared to $0.2 million for the same period of 2002. Research and development costs are composed primarily of costs related to the Company's efforts to gain FDA approval for the Isolagen Process in the United States. These costs include those personnel and laboratory costs related to the current FDA trials and certain consulting costs. This project is still under development. The total cost of research and development as of March 31, 2003 is $4.4 million. As of March 31, 2003, we believe at a minimum it will cost $3.6 million to complete this project. That estimate assumes that no further testing requirements are imposed by the FDA, that FDA approval is forthcoming and that FDA approval is received during 2005. The FDA approval process is extremely complicated and is dependent upon our study protocols and the results of our studies. In the event that the FDA requires additional studies or requires changes in our study protocols or in the event that the results of the studies are not consistent with our expectations the process will be more expensive and time consuming. Due to the vagaries of the FDA approval process we are unable to predict what the cost of obtaining approval will be if FDA approval is not forthcoming in 2005. The Company has other research projects currently underway, including those related to repairing damaged nerves and therapies to regrow hair and to heal burned skin. However, research and development costs related to these projects were not material during the 2003 or 2002 periods. The major components of the approximately $0.4 million increase in research and development expense are as follows: a) salaries increased by approximately $0.2 million to $0.3 million for the three months ended March 31, 2003 compared to

$0.1 million for the three months ended March, 2002; and b) laboratory expense increased by approximately $0.1 million to $0.1 million for the three months ended March 31, 2003 compared to $0.0 million for the three months ended March 31, 2002.

INTEREST INCOME. Interest income increased 64%, or $2,892, to $7,430 for the three months ended March 31, 2003 compared to $4,538 for the three months ended March 31, 2002. The increase in interest income may be attributed to, among other things, an increase in the amount of cash on hand by the Company, and an increase in interest rates paid on the Company's deposits.

OTHER INCOME. Other income of $55,663 for the three months ended March 31, 2003 represents gains realized on the sale of certain interest bearing securities denominated in Australian dollars and British pounds held to mitigate a portion of the foreign currency exposure related to the Company's international activity. As of March 31, 2003, the Company holds no such securities.

NET LOSS. Net loss for the three months ended March 31, 2003 was $2,189,101, as compared to a net loss of $746,538 for the three months ended March 31, 2002. This increase in net loss is attributed primarily to salaries, travel, consulting, legal, and promotional expenses. Net loss attributable to common stockholders for the three months ended March 31, 2003 was $2,398,883, as compared to a net loss of $746,538 for the three months ended March 31, 2002. These amounts include $0.2 million and $0.0 million of preferred stock dividends for the three months ended March 31, 2003 and March 31, 2002, respectively.



LIQUIDITY AND CAPITAL RESOURCES

Operating Activities

Cash used in operating activities during the three months ended March 31, 2003, amounted to $2,234,138, as compared to the $548,852 of cash used in operating activities during the three months ended March 31, 2002. The increase is attributed primarily to salaries, travel, consulting, legal, and promotional expenses.

Investing Activities

Cash used by investing activities during the three months ended March 31, 2003, amounted to $772,123 as compared to cash used by investing activities of $4,201 during the three months ended March 31, 2002. This increase in cash used is due to the purchase of property and equipment for the Houston, Texas, London, England, and Sydney, Australia laboratories.

Financing Activities

Cash provided by financing activities during the three months ended March 31, 2003, amounted to $92,400 raised from the issuance of common stock as compared to cash provided by financing activities of $0 during the three months ended March 31, 2002.

Working Capital

As of March 31, 2003, the Company had a cash balance of $1,352,584. As of May 5, 2003, the Company had a cash balance of approximately $0.6 million. The Company does not have any credit facilities with which to fund ongoing working capital needs. On May 9, 2003, the Company sold 110,250 shares of Series B Convertible Preferred Stock for a gross amount of approximately $3.1 million.

After deducting the costs and expenses associated with the sale, the Company received approximately $2.8 million. The long-term viability of the Company is dependent upon successful operation of its business and the ability to raise additional debt and equity within the near future.

Inflation did not have a significant impact on the Company's results during the three months ended March 31, 2003.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our market risk as it relates to foreign currency transactions is described in Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

ITEM 4. CONTROLS AND PROCEDURES

In accordance with Item 307 of Regulation S-K promulgated under the Securities Act of 1933, as amended, and within 90 days of the date of this Quarterly Report on Form 10-Q, the Chief Executive Officer and Chief Financial Officer of the Company (the "Certifying Officers") have conducted evaluations of the Company's disclosure controls and procedures. As defined under Sections 13a-14(c) and 15d-14(c) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), the term "disclosure controls and procedures" means controls and other procedures of an issuer that are designed to ensure that information required to be disclosed by the issuer in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by an issuer in the reports that it files or submits under the Exchange Act is accumulated and communicated to the issuer's management, including its principal executive officer or officers and principal financial officer or officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure. The Certifying Officers have reviewed the Company's disclosure controls and procedures and have concluded that those disclosure controls and procedures are effective as of the date of this Quarterly Report on Form 10-Q. In compliance



with Section 302 of the Sarbanes-Oxley Act of 2002, (18 U.S.C. 1350), each of the Certifying Officers executed an Officer's Certification included in this Quarterly Report on Form 10-Q.

As of the date of this Quarterly Report on Form 10-Q, there have not been any significant changes in the Company's internal controls or in other factors that could significantly affect these controls subsequent to the date of their evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

PART II - OTHER INFORMATION

ITEM 2. CHANGES IN SECURITIES AND USE OF PROCEEDS

In the first quarter of 2003, the Company issued 100,000 shares of its Common Stock to Pacgen Partners, a California general partnership. No broker or underwriter was involved in the issuance of the shares of Common Stock to Pacgen. These shares were issued to Pacgen in connection with the Company's purchase of two patent-pending in accordance with that certain Intellectual Property Purchase Agreement dated as of January 31, 2003 among the Company, Gregory M. Keller, M.D. and Pacgen Partners. The two patent-pending purchased by the Company are unrelated to the Isolagen Process currently being exploited by

the Company, but rather, in the Company's belief, are related to future potential applications for the Isolagen Process. The Company estimated that the two patent-pending which it purchased had, at the time of the purchase and sale was consummated, an aggregate value of approximately $540,000. Pacgen represented to the Company that it was, at the time the shares were issued, an "accredited investor" within the meaning of the rules issued under the Securities Act of 1933, as amended, and therefore the Company issued the shares of Common Stock in reliance on Regulation D promulgated under the Securities Act of 1933, as amended.

ITEM 5. OTHER INFORMATION

On May 9, 2003, the Company sold 110,250 shares of Series B Convertible Preferred Stock at $28.00 per share for a gross amount of approximately $3.1 million. Each share of Series B Convertible Preferred Stock is convertible into eight shares of the Company's common stock, at any time at the option of the holder of such shares. The Series B Convertible Preferred Stock accrues dividends at 6% per annum payable in cash or additional shares of Series B Convertible Preferred Stock. Fordham Financial Management, Inc. acted as the Company's placement agent in connection with the offer and sale of the Series B Convertible Preferred Stock. After deducting the aggregate costs and expenses associated with the offer and sale of the shares of the Series B Convertible Preferred Stock, the Company actually received approximately $2.8 million. The Company also issued to Fordham Financial Management, Inc. a warrant to purchase 88,200 shares of the Company's common stock for a purchase price of $3.50 per share (subject to adjustment from time to time in accordance with the terms of the warrant).

ITEM 6. EXHIBITS AND REPORTS

(A) EXHIBITS

| EXHIBIT NO. | IDENTIFICATION OF EXHIBIT |
|---|---|
| 4.3 | Certificate of Designation of Series B Convertible Preferred Stock filed with the Delaware Secretary of State on May 8, 2003 (incorporated by reference to Exhibit 4.3 of the Registrant's Form 10-Q for the quarter ended March 31, 2003) |
| 4.4 | Form of Warrant issued to Fordham Financial Management, Inc. (incorporated by reference to Exhibit 4.4 of the Registrant's Form 10-Q for the quarter ended March 31, 2003) |
| 31.1 | Certification of Chief Executive Officer pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |



| | |
|---|---|
| 31.2 | Certification of Chief Financial Officer pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the |

Sarbanes-Oxley Act of 2002.

| | |
|---|---|
| 32.1 | Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| 32.2 | Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |



SIGNATURES

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

ISOLAGEN, INC.

Date: November 10, 2003

By: /s/ Jeffrey W. Tomz
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Jeffrey W. Tomz, CFO and Secretary
(Principal Executive and
Financial Officer)



Exhibit Index

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|---|---|
| 31.2 | Certification of Chief Financial Officer pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 32.1 | Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| 32.2 | Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |