

Annual Report
December 31, 2015

www.scilearn.com

2015 Chairman Letter

We are thrilled to report that the momentum for our unique solutions continues to build, enabling us to achieve our first year of sales growth since 2009. Most importantly, we continue to remove numerous obstacles in the transition to our new business model while gaining substantial leverage on our growing sales across all four segments of our business. We continue to be encouraged about the rapidly expanding interest in our neuroscience learning innovations particularly for students of poverty along with our focus on Special Education, RTI 3, and ELL learners. This focus is concentrated on the students who struggle the most and for which the achievement gap continues to widen. Research from universities and school districts continue to confirm what our founding scientists discovered more than 30 years ago; the brain can be changed fast at the neurological level, and these changes produce significant improvement in foundation cognitive skills, language skills, and literacy performance. Equally important, these improved results are sustained over time, which supports the critical goal of no summer loss.

We also made immense progress in executing critical elements of our strategic and operating plan, including a 4% sales increase in Q4 2015 compared to Q4 2014 and a 5% increase for the year compared to 2014. Another critical element of our operating plan was realizing positive free cash flow in order to establish a solid base for 2016. We exceeded the 2015 goal by a remarkable 60%, realizing over $0.7 million in free cash flow. Our subscription sales grew 4% for the year compared to 2014, and as of December 31, 2015 over 70% of our sales are recurring. In addition, our Private Provider and Consumer/BrainPro business segments experienced double digit sales growth for the year while International sales also showed growth despite a tough global economic environment. Our teams continue to reduce costs while getting more done with less. This is evident in our business achieving a 26% year over year improvement in operating profitability.

Our employees remain focused on our critical mission of bringing advances in neuroscience research and technology to bear on learners struggling around the world. We also made excellent progress in releasing more product options to our customers and perspective buyers. We now provide all Fast ForWord® and Reading Assistant® products on the iPad®, Chrome Browser, and Chromebook platforms. With our solutions now available on all of the most common platforms, along with additional tools for the administrators, and a high performing, scalable technology platform, we are positioned to maintain our business on a sustainable and profitable growth path in 2016 and years beyond.

The fourth quarter was our third consecutive quarter of sales growth. New sales continued to improve with K-12 new business sales up 20% over Q4 2014 and a 14% increase for the full year compared to 2014. As evidenced by the increasing momentum in sales, our lead generation engine demonstrated growing demand with 45,000 new K-12 leads and 10,000 Consumer leads generated in 2015. Renewals were strong in the quarter as well and we made solid progress for the year.

As previously mentioned, we are pleased to have released our Reading Assistant program on the iPad®, Chrome Browser, and Chromebook platforms. Our customers are particularly excited about the use of touch technology with younger students and the results they achieve in building critical foundational cognitive skills. Adding even more optional protocols has also offered teachers and schools more flexibility in scheduling. Also, the addition of a tool to assist our largest districts with mass student updates has been a big hit, enabling the districts and schools to automate the movement of students primarily at the beginning of a new school year as well as at the semester break. These achievements and others were attained without adding any additional development resources during the year. These advances with our solutions are enabling us to reach more learners and providing the teachers and coaches more tools to help those students that are struggling.

Since starting our first ever free trial program in September, we have seen tremendous response in signups for new districts and schools. This has been one of our most successfully planned and executed campaigns, as evidenced by the over 1,100 new prospects who signed-up to try our solution at no charge for four months. This will allow K-12 educators to observe the power of Fast ForWord to quickly impact students' academic performance as well as their behavior. We anticipate this trial program to reach 1,500 by the end of Q1 2016, generating high quality leads and growing our 2016 pipeline. Even a modest conversion rate could have a significant impact on sales in 2016.

The competitive bid we were awarded from the State of Arizona for an ELL Pilot Project involving 7,000 students is now scheduled to get started this July and will span two years. We are very pleased to be working with the State of Arizona to

demonstrate the power of our neuroscience-based intervention to wire the brain for English and then to provide individualized fluency practice in English with corrective feedback for each ELL learner. Typically, it takes non-English speakers seven or more years to master English using traditional English language development approaches, while our partners across Asia, as well as customers in the U.S., are demonstrating that non-English speakers can often become fluent in three years or less using our solutions.

Our new partnership with Eric Jensen Learning started in September and we have seen great response from educators, including tremendous demand for our first webinar in February and first Brain Summit in Atlanta in March. Dr. Eric Jensen is a very strong voice amongst teachers and educational leaders on the importance of neuroplasticity in improving student performance and a sought after presenter and renowned writer. He has written a number of books, including "Teaching with Poverty in Mind," which conveys the impact of poverty on the brain but then provides a compelling road map for how teachers and educational leaders can reach these students to provide a path out of poverty. In his books and presentations, Dr. Jensen calls out many of the research studies about our solutions as well as citing Fast ForWord and Reading Assistant as great examples of applying neuroscience research in practical applications for teachers to use in the classroom. We have scheduled several events in 2016 featuring Dr. Jensen. Along with Dr. Jensen, our goal is to continue to raise awareness about the power and necessity of neuroplasticity in reaching students who struggle the most.

The U.S. K-12 funding environment continues to improve for most states, and federal funding is stable. We are pleased that ESEA was re-authorized and maintains concentration on subgroups that include our focus areas of Special Education, ELL, and students of poverty. This is a major source of funding for our interventions. This improved environment is evident in our pipelines, which continue to be solid with improving quality as our sales organization matures and our marketing programs continue to be focused in Special Education, RTI 3, and ELL. Additionally, our message of FAST and ENDURING results is gaining traction because of its uniqueness and the exceptional research that allows us to make this claim. We are also gaining traction in a third dimension of this message, poverty. There are a tremendous number of neuroscience research studies gaining national attention on the impact of poverty on the brain. We are finding that educational leaders and teachers are very interested in examining our solution in the context of poverty and exploring how cognitive interventions help these students close the achievement gap rapidly by quickly improving foundational skills.

The MySciLearn platform is scaling beautifully and delivering consistent and reliable access to our learning innovations anywhere, anytime. Today, more than 2.6 million learners have used Scientific Learning software products; and since the introduction of MySciLearn in late 2011, over 500,000 learners have used our products online.

Our BrainPro solution sold directly to parents with children that have language impairments, dyslexia, or autism continues to grow rapidly with sales up 7% over Q4 2014 and 10% for the full year compared to 2014. This marks our third consecutive year of growth and demonstrates the unmet need and demand for our unique, neuroscience based solutions. During 2015, we also successfully improved the operating margins for this segment.

International sales were up 3% over Q4 2014 and up 1% over the full year 2014, respectively, an impressive three years of consecutive sales growth. We now have over 55 countries using our unique solutions. The largest percentage of our sales come from Asia where our learning innovations are used to quickly accelerate English Language proficiency and it is clear that these rapid changes are sustained over time.

Also, our Private Provider (clinical) segment had a positive quarter with sales up 13% over Q4 2014 and a remarkable 11% for the full year compared to 2014, marking our first year of growth in the Private Provider segment since 2008.

Our strategic direction is working and creating increasing momentum. We are narrowing our focus on the students who are not prepared to fully participate in a rigorous academic environment. These are primarily students classified as living at or below the poverty line and/or with specific learning disabilities, autism and/or English Language Learners. Our solutions produce fast and enduring results among the students most in need of help. Additionally, our non K-12 segments (Consumer/Brain Pro, International, and Private Provider) are focused on these same students producing important alignment across all market segments we are targeting.

We have established a 2016 operational plan that aligns our resources and teams to execute this focus and have tactics in place. These tactics include successfully converting our free trial participants to new sales, continuing to improve our

sales productivity, expanding our existing district customer base, and leveraging our partnership with Eric Jensen, all in order to reach those students in greatest need of our solutions. Our 2016 operating plan is focused on maintaining our K-12 business sales growth momentum with the increase coming again in the second half of the year.

Financial Highlights:

- Booked sales for the fourth quarter of 2015 were $3.9 million compared to $3.7 million in the fourth quarter of 2014 and $17.6 million for the full year ended December 31, 2015 compared to $16.8 million in 2014.
    - K-12 booked sales were $3.0 million for the fourth quarter of 2015 and $14.0 million for the year, increases of 4% and 5% over 2014, respectively. We are extremely pleased with the progress in K-12, returning to growth for the first year since 2009, particularly in new sales. For comparison, we experienced 35%, 28%, and 8% year over year declines in 2012, 2013, and 2014, respectively. We are anticipating continued growth in K-12 in 2016, primarily in the second half of the year.
    - Non-K-12 booked sales increased 7% for the fourth quarter of 2015 compared to the fourth quarter of 2014 and 3% to $3.5 million for the year ended December 31, 2015. The increase for the year is driven by growth in each of our Private Provider, International, and Consumer/BrainPro businesses. We are anticipating continued growth from each of these business segments in 2016.
- Revenue decreased by 10% for the fourth quarter of 2015 and 8% for the year ended December 31, 2015 compared to the corresponding periods in 2014, driven by a higher sales mix of subscription sales, lower renewal sales, and less on-site service deliverables. Subscription revenues are now 41% of revenue as of December 31, 2015, as compared to 36% in 2014.
- Operating income in the fourth quarter of 2015 was $0.04 million and $1.0 million for the year ended December 31, 2015 compared to $0.4 million and $0.8 million in the corresponding periods in 2014. The 2015 improvement of 26% was driven primarily by solid expense management in 2015. The fourth quarter of 2015 was our second consecutive quarter of operating profit and 2015 was our second consecutive year with operating profit. These results demonstrate the operating leverage being gained with a modest growth in sales.
- Net income in the fourth quarter of 2015 was $0.4 million and net loss of $0.2 million for the year ended December 31, 2015 compared to net income of $0.4 million and $1.4 million in the corresponding periods in 2014. The lower net income for the year was driven by $1.3 million in patent sales in 2014 along with a $0.7 million increase in warrant valuation expense in 2015.
- We finished the year with over $3.5 million in cash compared to $2.0 million 2014. We generated over $0.7 million in free cash flow, well above our operating plan and an 87% improvement over 2014. On April 6, 2015, we refinanced our subordinated debt and raised $5 million in new subordinate debt securities. The new subordinated debt matures in 3 years on April 6, 2018 and the proceeds were used for the repayment of outstanding subordinated debt plus working capital and general corporate purposes. We also renewed our line of credit with Bridge Bank.

We remain convinced that Scientific Learning has the necessary ingredients for success. We have a suite of unique, patented learning innovations that produce fast and lasting results. These solutions are now delivered on our robust on-demand platform anytime, anywhere, and we have added the iPad, Chrome Browser, and Chromebook platforms as additional delivery options. We have expanded our administration tools to further enable our users to optimize use of our products. We are serving markets with urgent need and growing accountability requirements. We have talented, dedicated employees committed to our important work. We have significantly reduced and aligned our cost structures to fit our transformation of the business model. Customer satisfaction is up, and more students each day are accessing our solutions on mobile technology as well as using more flexible protocols. We have and continue to take the necessary action to strengthen our balance sheet. We must continue to improve sales productivity through the expansion of our existing customers; improve our renewal rate; and adding more new school districts. We remain optimistic about the future.

Attached to this letter are our financial statements for the period ending December 31, 2015 as well as the disclosures according to the OTC Disclosure guidelines.

Your continued interest and support is most appreciated.

Robert C. Bowen
Chairman and Chief Executive Officer

Forward-Looking Statements

This letter contains forward-looking statements. Such statements are subject to substantial risks and uncertainties. Actual events or results may differ materially as a result of many factors, including but not limited to: anticipated future sales and financial results, general economic and financial conditions (including current adverse conditions in government budgets and the general economy); availability of funding to purchase the Company's products and generally available to schools, including the amount and duration of federal and state funding; the acceptance of new products and product changes in existing and new markets; acceptance of subscription and other recurring offerings; seasonality and sales cycles in Scientific Learning's markets; competition; the extent to which the Company's development, marketing, sales and implementation strategies are successful; the results from the Company's free trial program; personnel changes; and the Company's ability to continue to demonstrate the efficacy of its products. The Company disclaims any obligation to update information contained in these forward-looking statements, whether as a result of new information, future events, or otherwise.

FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

INDEPENDENT AUDITOR'S REPORT ON THE CONSOLIDATED FINANCIAL STATEMENTS

To the Board of Directors
Scientific Learning Corporation
Oakland, California

We have audited the accompanying consolidated financial statements of Scientific Learning Corporation (a Delaware corporation) which comprise the consolidated balance sheets as of December 31, 2015 and 2014, and the related consolidated statements of operations, comprehensive income (loss), stockholders' deficit and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Scientific Learning Corporation as of December 31, 2015 and 2014, and the results of their operations and their cash flows for the years then ended.

/s/ Armanino LLP

San Ramon, California
March 3, 2016

SCIENTIFIC LEARNING CORPORATION
CONSOLIDATED BALANCE SHEETS
(In thousands, except share and per share data)

	December 31, 2015	December 31, 2014
Assets		
Current assets:		
Cash and cash equivalents	$ 3,513	$ 2,032
Accounts receivable, net of allowance for doubtful accounts of $14 and $21, respectively	1,390	1,831
Prepaid expense and other current assets	721	1,097
Total current assets	5,624	4,960
Property and equipment, net	667	465
Other assets	156	33
Total assets	$ 6,447	$ 5,458
Liabilities and stockholders' deficit		
Current liabilities:		
Accounts payable	$ 41	$ 257
Accrued liabilities	1,348	1,399
Deferred revenue	7,832	7,873
Total current liabilities	9,221	9,529
Deferred revenue, net of current	224	363
Subordinated debt	4,830	4,092
Warrant liability	903	226
Other liabilities	96	107
Total liabilities	15,274	14,317
Commitments and contingencies (see Note 15 to the consolidated financial statements)		
Stockholders' deficit:		
Common stock $0.001 par value: 40,000,000 authorized, 24,344,001 and 24,068,870 shares issued and outstanding as of December 31, 2015 and December 31, 2014, respectively, and additional paid-in capital	97,240	97,002
Accumulated deficit	(106,062)	(105,857)
Accumulated other comprehensive loss	(5)	(4)
Total stockholders' deficit	(8,827)	(8,859)
Total liabilities and stockholders' deficit	$ 6,447	$ 5,458

See accompanying notes to consolidated financial statements.

SCIENTIFIC LEARNING CORPORATION
CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share data)

	Year Ended December 31,	
	2015	**2014**
Revenues:		
Subscription	$ 7,221	$ 6,955
License	3,509	3,199
Service and support	7,000	9,017
Total revenues	17,730	19,171
Cost of revenues:		
Cost of subscription	836	1,044
Cost of license	97	121
Cost of service and support	2,555	2,887
Total cost of revenues	3,488	4,052
Gross profit	14,242	15,119
Operating expenses:		
Sales and marketing	7,275	8,068
Research and development	2,398	2,400
General and administrative	3,555	3,847
Total operating expenses	13,228	14,315
Operating income	1,014	804
Interest and other income (expense), net	(1,215)	628
Income (loss) before provision for income tax	(201)	1,432
Provision for income taxes	4	16
Net income (loss)	$ (205)	$ 1,416
Net income (loss) per share:		
Basic	$ (0.01)	$ 0.06
Diluted	$ (0.01)	$ 0.06
Weighted average shares used in computing net income (loss) per share:		
Basic weighted average shares outstanding	24,204	23,769
Effect of dilutive securities:		
Employee stock options and awards	-	20
Diluted weighted average shares outstanding	24,204	23,789

See accompanying notes to consolidated financial statements.

SCIENTIFIC LEARNING CORPORATION
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(In thousands)

	Year Ended December 31,	
	2015	**2014**
Net income (loss)	$ (205)	$ 1,416
Other comprehensive loss:		
Foreign currency translation adjustments, net of tax	(1)	-
Comprehensive income (loss)	$ (206)	$ 1,416

See accompanying notes to consolidated financial statements.

SCIENTIFIC LEARNING CORPORATION
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' DEFICIT
(In thousands, except share amounts)

	Common Stock and Additional Paid-In Capital		Accumulated Deficit	Other Comprehensive Loss	Stockholders' Deficit
	Shares	Amount			
Balance at December 31, 2013	**23,873,705**	**$ 96,642**	**$ (107,273)**	**$ (4)**	**$ (10,635)**
Issuance of common stock under employee stock purchase plan	88,758	11	-	-	11
Stock-based compensation expense	-	350	-	-	350
Vesting of restricted stock units	112,094	-	-	-	-
Tax withholding related to vesting of restricted stock units	(5,687)	(1)	-	-	(1)
Currency translation adjustment	-	-	-	-	-
Net Income	-	-	1,416	-	1,416
Balance at December 31, 2014	**24,068,870**	**$ 97,002**	**$ (105,857)**	**$ (4)**	**$ (8,859)**
Grants of restricted stock awards	200,000	-	-	-	-
Stock-based compensation expense	-	239	-	-	239
Vesting of restricted stock units	82,565	-	-	-	-
Tax withholding related to vesting of restricted stock units	(7,434)	(1)	-	-	(1)
Currency translation adjustment	-	-	-	(1)	(1)
Net loss	-	-	(205)	-	(205)
Balance at December 31, 2015	**24,344,001**	**$ 97,240**	**$ (106,062)**	**$ (5)**	**$ (8,827)**

See accompanying notes to consolidated financial statements.

SCIENTIFIC LEARNING CORPORATION
CONSOLIDATED STATEMENT OF CASH FLOWS
(In thousands)

	Year Ended December 31, 2015	2014
Operating Activities:		
Net income (loss)	$ (205)	$ 1,416
Adjustments to reconcile net income (loss) to cash provided by (used in) operating activities:		
Depreciation and amortization	341	798
Stock based compensation expense	239	350
Paid-in-kind interest expense	-	151
Amortization of debt discount and deferred debt issuance cost	217	384
Increase (decrease) in fair value of warrant	416	(269)
Gain on sale of patents	-	(1,337)
Changes in operating assets and liabilities:		
Accounts receivable	441	426
Prepaid expenses and other current assets	348	(467)
Other assets	(100)	555
Accounts payable	(216)	(37)
Accrued liabilities	(51)	(361)
Deferred revenue	(181)	(2,349)
Other liabilities	1	99
Net cash provided by (used in) operating activities	1,250	(641)
Investing Activities:		
Purchases of property and equipment and additions to capitalized software	(531)	(312)
Net proceeds from patent sale	-	1,337
Net cash provided by (used in) investing activities	(531)	1,025
Financing Activities:		
Borrowings under bank line of credit	232	-
Repayment of borrowings under bank line of credit	(232)	-
Repayment of borrowings under subordinated debt	(4,177)	(1,000)
Payments under capital lease	(12)	-
Proceeds from exercise of options and employee stock purchase plan	-	11
Proceeds from issuance of subordinated debt	5,000	-
Debt issuance cost	(47)	-
Net settlement of common stock	(1)	(1)
Net cash provided by (used in) financing activities	763	(990)
Effect of exchange rate changes on cash and cash equivalents	(1)	-
Increase (decrease) in cash and cash equivalents	1,481	(606)
Cash and cash equivalents at beginning of period	2,032	2,638
Cash and cash equivalents at end of period	$ 3,513	$ 2,032
Supplemental disclosure of cash flow information		
Cash paid for income taxes	$ 18	$ 7
Cash paid for interest	$ 571	$ 373
Non-cash financing activities		
Capital lease	$ 30	$ 62
Fair value of common stock warrants issued in connection with subordinated debt financing	$ 261	$ -

See accompanying notes to consolidated financial statements.

Notes to Consolidated Financial Statements

1. Summary of Significant Accounting Policies

Description of Business

Scientific Learning Corporation (the "Company") develops, distributes and licenses technology that accelerates learning by improving the processing efficiency of the brain.

The Company's patented products build learning capacity by rigorously and systematically applying neuroscience-based learning principles to improve the fundamental cognitive skills required to read and learn. To facilitate the use of the Company's products, the Company offers a variety of on-site and remote professional and technical services, as well as phone, email and web-based support. The Company sells primarily to K-12 schools in the United States through a direct sales force.

All of the Company's activities are in one operating segment.

The Company was incorporated in 1995 in the State of California and was reincorporated in 1997 in the State of Delaware.

Principles of Consolidation and Basis of Presentation

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary in Shanghai, China. All significant intercompany balances and transactions have been eliminated in consolidation.

Use of Estimates

The preparation of financial statements, in conformity with accounting principles generally accepted in the United Sates ("U.S. GAAP"), requires management to make certain estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the financial statements as well as the reported amounts of revenues and expenses during the periods presented. To the extent that there are material differences between these estimates and actual results, the Company's consolidated financial statements could be affected.

Revenue Recognition

The Company derives revenue from the sale of licenses to its software and from professional service and support fees. Software license revenue is recognized in accordance with accounting standards for software companies. Additionally, the Company derives revenue from subscription fees for access to and use of its on-demand application services. Under the Company's subscription arrangements for its on-demand application services, the customer does not have the contractual right to take possession of the software at any time during the subscription period. Thus, revenue for the Company's subscription services is recognized in accordance with accounting standards for service contracts.

There are four basic criteria which must be met to recognize revenue. These are: 1) persuasive evidence of an arrangement exists; 2) delivery of the product has occurred; 3) a fixed or determinable fee; and 4) the collection of the fee is reasonably assured. The application of the relevant accounting standards requires the Company to exercise significant judgment related to specific transactions and transaction types. In cases where extended payment terms are granted to school customers, the Company determines if the fixed or determinable fee criterion is met by reference to the customer's specific funding sources, especially where the payment terms extend into the customer's next fiscal year. If the Company determines that the fixed or determinable fee criterion is not met at the inception of the arrangement, the Company defers revenue recognition until the payments become due.

The value of software licenses, subscriptions, professional services and support invoiced during a particular period is recorded as deferred revenue until recognized. All revenue from transactions that include software licenses for new products that have not yet been delivered is deferred until the delivery of all products. Direct costs related to deferred software license revenue are deferred until the related license revenue is recognized.

Multiple contracts with the same customer are generally accounted for as separate arrangements, except in cases where contracts are so closely related that they are effectively part of a single arrangement.

Multiple-element software arrangements

Booked sales of software to the Company's school customers typically include multiple elements (e.g., Fast ForWord perpetual software licenses, support, training, implementation management, and other professional services). The Company recognizes software revenue using the residual method, whereby the difference between the total arrangement fee and the total "vendor specific objective evidence" ("VSOE") of fair value of the undelivered elements is recognized as revenue relating to the delivered elements. VSOE of fair value for each element of an arrangement is based upon the normal pricing and discounting practices for those products and services when sold separately and, for support services, is also measured by the renewal price. The Company is required to exercise judgment in determining whether VSOE of fair value exists for each undelivered element based on whether the pricing for these elements is sufficiently consistent.

Multiple-element on-demand application service arrangements

Booked sales of subscriptions to the Company's on-demand application services can also include multiple elements similar to software arrangements. The Company follows accounting guidance for revenue recognition of multiple-element arrangements to determine whether such arrangements contain more than one unit of accounting. Multiple-element arrangements require the delivery or performance of multiple products, services and/or rights to use assets. To qualify as a separate unit of accounting, the delivered item must have value to the customer on a standalone basis and revenue is allocated to each deliverable in the arrangement based on the relative fair value of the respective deliverable. The Company's on-demand subscription services, support, training and implementation management services have standalone value as these services are sold separately by the Company, and the Company has established VSOE of fair value for determining the fair value of each element.

Multiple-element arrangements—arrangements with software and non-software elements

Booked sales may include a combination of software related and non-software related products and services offerings including on-demand subscription services, perpetual software licenses, support, training, implementation management, and other professional services. In such arrangements, the Company first allocates the total arrangement consideration based on the relative selling prices of the software group of elements as a whole and to the non-software elements. The Company then further allocates consideration within the software group to the respective elements within that group following the software revenue guidance as prescribed by U.S. GAAP.

Subscription revenue

Subscription revenue primarily includes revenue from annual or monthly customer subscriptions to our web-based applications, including Fast ForWord, Reading Assistant, and BrainPro. Subscription revenue is recognized as follows:

• On-demand application services – revenue for subscription services is recognized ratably over the term of the subscription period.
• Per student per month – student usage of any of our products during a calendar month. Revenue is recognized monthly over the period of use.

• Individual participant subscriptions – software subscriptions for a single participant. Revenue is recognized ratably over the term of the subscription period.

License revenues

License revenue primarily includes revenue from the sales of perpetual licenses to our software applications including Fast ForWord and Reading Assistant. License revenue is recognized as follows:

• Perpetual licenses – software licensed on a perpetual basis. Revenue is recognized at the later of product delivery date or contract start date using the residual method. If VSOE of fair value does not exist for all the undelivered elements, all revenue is deferred and recognized ratably over the service period if the undelivered element is services or when all elements have been delivered.

• Software term licenses – software licensed for a specific time period, generally a term of one to three years. Revenue is recognized ratably over the license term.

Professional service and support revenue

Professional service and support revenue is derived from a combination of training, implementation, technical and professional services, online services and customer support. Training, implementation, technical and other professional services are typically sold on a per day basis. Professional services revenue is recognized as performed. Online service and customer support are recognized ratably over the service period. If VSOE does not exist for all the elements in a software arrangement except software licenses, service revenue is recognized over the longest contractual period in an arrangement. Revenue from services sold alone or with support is recognized as performed.

Cash and Cash Equivalents

Cash and cash equivalents, which consist of cash on deposit with banks and money market accounts, are stated at fair value.

Accounts Receivable and Allowance for Doubtful Accounts

The Company conducts business primarily with public school districts and speech and language professionals in the United States. The Company records accounts receivable at the invoiced amount and the Company does not require collateral. The Company maintains an allowance for doubtful accounts for estimated losses due to the inability of customers to make payments. The allowance is determined based on any specific reserves deemed necessary and the Company's historical experience of bad debt write-offs.

Deferred Charges

The Company defers royalty charges as incurred and recognizes the expense over the term of the related license agreements or service periods. These deferred charges are included in prepaid expenses and other current assets in the consolidated balance sheets.

Property and Equipment

Property and equipment is recorded at cost. Depreciation is computed using the straight-line method over the estimated useful lives of the assets, which range from three to five years. For leased assets and leasehold improvements, depreciation is computed using the straight-line method over the shorter of the lease or the estimated useful life.

Software and Website Development Costs

The Company capitalizes certain software development costs incurred subsequent to the establishment of technological feasibility and amortizes those costs over the estimated lives of the related products. The annual amortization is computed using the straight-line method over the remaining estimated economic life of the product. Technological feasibility is established upon completion of a working model. These capitalized costs are included in property and equipment in the consolidated balance sheets. Software development costs were insignificant for the years ended December 31, 2015 and 2014.

The Company also capitalizes costs related to internal-use software and website application, infrastructure development and content development costs. Costs related to preliminary project activities and post-implementation activities were expensed as incurred. Internal-use software is amortized on a straight-line basis over its estimated useful life, generally three years. The capitalized costs are included in property and equipment in the consolidated balance sheets. For the years ended December 31, 2015 and December 31, 2014, the company capitalized $0.3 million and $0.2 million of internal-use software and website development costs, respectively.

The Company evaluates the useful lives of these assets on an annual basis and tests for impairment whenever events or changes in circumstances occur that could impact the recoverability of these assets. If indicators of impairment are present, estimates of future cash flows are used to test the recoverability of the asset. If the carrying amount of the asset exceeds its fair value, an impairment charge is recognized.

Interest and Principal

The Company accrues payment-in-kind interest. It is the amount of principal and interest payable related to the subordinated debt financing completed on April 5, 2013. From the issuance date through the first anniversary thereof, the Company accrued interest and increased the principal. See Note 9 to the consolidated financial statements.

Debt discount and debt issuance costs

The Company recorded a debt discount and debt issuance costs related to the subordinated debt issued on April 5, 2013 and on April 6, 2015. These costs are being amortized to interest expense over the life of the debt. The debt discount and debt issuance costs in relation to the 2013 subordinated debt were fully amortized at December 31, 2015. The debt discount and debt issuance cost in relation to the 2015 subordinated debt refinance were capitalized in long term debt and other assets, respectively. In addition, the Company amortizes the debt issuance costs over the life of the debt. See Note 9 to the consolidated financial statements.

Long-Lived Assets

Long-lived assets, such as property and equipment and purchased intangible assets subject to amortization are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. The recoverability of an asset is measured by a comparison of the carrying amount of an asset to its estimated undiscounted future cash flows. If the carrying amount of an asset exceeds its estimated undiscounted future cash flows, an impairment charge is recognized for the amount by which the carrying amount of the asset exceeds the fair value of the

asset. For the years ended December 31, 2015 and December 31, 2014, the Company recorded zero of impairment charges related to long-lived assets, respectively.

Fair Value of Financial Instruments

The carrying amounts of cash equivalents, accounts receivable and accounts payable approximate fair value as they are short-term in nature or have relatively short maturities.

Concentration of Risk

Financial instruments that are potentially subject to concentrations of credit risk consist principally of cash equivalents and accounts receivable.

Cash and cash equivalents are primarily held in a major financial institution in the United States. Such deposits may be in excess of insured limits and are not insured in other jurisdictions. The Company believes that the financial institution that holds the Company's cash and cash equivalents is financially sound and, accordingly, minimal credit risk exists with respect to these assets.

Accounts receivable are primarily from sales to customers located in the United States. The Company performs ongoing credit evaluations of customers. The Company does not require collateral.

An allowance for doubtful accounts is determined with respect to those accounts that have been determined to be doubtful of collection. There are three customers that accounted for an aggregate of 39% of accounts receivable balance as of December 31, 2015 and no customers accounted for more than 10% of accounts receivable balance as of December 31, 2014.

There were no customers that accounted for more than 10% of revenue for the years ended December 31, 2015 and 2014.

The Company has no off-balance sheet concentration of credit risk, such as foreign exchange contracts, option contracts or other hedging arrangements.

Concentration of sales in the K-12 market potentially exposes the Company to risk. Approximately 80% of our booked sales for the years ended December 31, 2015 and 2014 came from the K-12 market in the United States and Canada. That market is characterized by its dependence on federal funding and state and local tax revenues, a political environment, particularly when large transactions are involved and a generally conservative approach to change. All of these attributes, particularly in the current economic and political environment, can result in a time-consuming and unpredictable sales cycle for large transactions. Because of the concentration of our sales in this market, we are particularly exposed to its risks.

Accounting for Stock-Based Compensation

Stock-based compensation expense is recorded on a straight-line basis over the requisite service period and includes an estimate for forfeitures.

Advertising

Advertising costs are expensed as incurred. Advertising expenses were $0.1 million, and $0.07 million for the years ended December 31, 2015 and 2014, respectively.

Income Taxes

Deferred tax assets and liabilities are measured using enacted tax rates and laws that are expected to be in effect when the differences are expected to reverse. Valuation allowances are established when necessary to reduce deferred tax assets to the net amount expected to be realized.

Net Income (loss) per Share

Basic net income (loss) per share is computed using the weighted-average number of common shares outstanding during the period. Diluted net income (loss) per share reflects the potential dilution of securities by adding common stock equivalents (computed using the treasury stock method) to the weighted-average number of common shares outstanding during the period, if dilutive.

For the years ended December 31, 2015 and 2014, 1,701,201 and 1,868,169 stock options, respectively, were excluded from the calculation of diluted net income (loss) per share because their effect is anti-dilutive. For the years ended December 31, 2015 and 2014, 140,433 and 240,559 stock awards, respectively, were excluded from the calculation of diluted net income (loss) per share because their effect is anti-dilutive. For the years ended December 31, 2015 and 2014, common stock warrants exercisable for 7,352,792 and 4,352,792 shares of common stock, respectively, were excluded from the calculation of diluted net income (loss) per share because their effect is anti-dilutive.

Foreign Currency Translation

The functional currency of the Company's China subsidiary is the local currency, the Chinese Renminbi "RMB." Adjustments resulting from translating foreign functional currency financial statements into U.S. dollars are recorded as part of a separate component of stockholders' deficit. Foreign currency transaction gains and losses are included in interest and other income (expense), net. All assets and liabilities denominated in a foreign currency are translated into U.S. dollars at the exchange rate as of the balance sheet date. Revenues and expenses are translated at the average exchange rate during the period. Equity transactions are translated using historical exchange rates.

Recent Accounting Pronouncements

In May 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers (Topic 606*). This new standard will replace most existing U.S. GAAP guidance on this topic. The new revenue recognition standard provides a unified model to determine when and how revenue is recognized. The core principle is that a company should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration for which the entity expects to be entitled in exchange for those goods or services. This guidance will be effective for the Company beginning January 1, 2018 and can be applied either retrospectively to each period presented or as a cumulative-effect adjustment as of the date of adoption. The Company is evaluating the impact of adopting this new accounting standard on its consolidated financial statements and has not selected a transition method.

In January 2015, the FASB issued ASU No. 2015-01, *Income Statement - Extraordinary and Unusual Items (Subtopic 225-20): Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items.* The new

guidance eliminates the separate presentation of extraordinary items, net of tax and the related earnings per share, but does not affect the requirement to disclose material items that are unusual in nature or infrequently occurring. The ASU applies to all entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. Entities have the option to apply the new guidance prospectively or retrospectively, and can choose early adoption. The Company is currently assessing the impact of the adoption of this guidance on the consolidated financial statements.

In April 2015, the FASB issued ASU No. 2015-03, *Interest - Imputation of Interest (Subtopic 835-30) – Simplifying the Presentation of Debt Issuance Costs*. ASU 2015-03 simplifies the presentation of debt issuance costs by requiring that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct reduction from the carrying amount of that debt liability, consistent with debt discounts. The recognition and measurement guidance for debt issuance costs are not affected by this ASU. The amendments in this ASU are effective for financial statements issued for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. The adoption of this ASU by the Company will change the presentation of debt issuance costs, which will be reported as a direct offset to the applicable debt on the consolidated balance sheet.

In November 2015, the FASB issued an ASU No. 2015-17, *Income Taxes (Topic 740)*. ASU 2015-17 amends the accounting for income taxes and requiring all deferred tax assets and liabilities to be classified as non-current on the consolidated balance sheet. The ASU is effective for reporting periods beginning after December 15, 2016, with early adoption permitted. The ASU may be adopted either prospectively or retrospectively. The Company is currently evaluating the method of adoption.

In February 2016, the FASB issued ASU No. 2016-02, "*Leases (Topic 842)*," which requires lessees to recognize a right-of-use asset and lease liability for all leases with terms of more than 12 months. Recognition, measurement and presentation of expenses will depend on classification as a finance or operating lease. ASU 2016-02 is effective for the Company on December 15, 2018. The Company is currently assessing the impact of the adoption of this new accounting standard on the consolidated financial statements.

2. Warrant Liability

In connection with the Company's private common stock offering that closed on March 28, 2012, the Company issued warrants ("PIPE warrants") to purchase an aggregate of 2,505,852 shares of common stock. The warrants have an exercise price of $1.82 per share and expire five years from the date of issuance. In addition, the warrants contain a cash settlement provision that may be triggered upon request by the warrant holders if the Company is acquired or in the case of a merger event, as defined by the warrant agreement.

Additionally, in connection with the Company's subordinated debt financing completed on April 5, 2013, the Company issued warrants ("2013 Sub-debt warrants") to purchase an aggregate of 1,846,940 shares of common stock. The warrants have an exercise price of $1.03 per share and expire three years from the date of issuance. The warrants contain a cash settlement provision that may be triggered upon request by the warrant holders if the Company is acquired or in the event of a merger, as defined by the warrant agreement.

On April 6, 2015, in connection with the Company's re-financing of its subordinated debt, the Company issued warrants ("2015 Sub-debt warrants") to purchase an aggregate of 3,000,000 shares of the Company's common stock at an initial exercise price of $0.14 per share and expire five years from the date of issuance. The warrants contain a cash settlement provision that may be triggered upon request by the warrant holders if the Company is acquired or in the event of a merger, as defined by the warrant agreement.

Under the FASB Accounting Standards Codification ("ASC") Topic 815, *Derivatives and Hedging,* an equity contract that can be settled in cash at the request of the holder must be classified as an asset or a liability. The accounting guidance also requires that the warrants be re-measured at fair value at each reporting date, with the change in fair value recorded in the Company's consolidated statement of operations. See Note 3 to the consolidated financial statements.

As of December 31, 2015 and 2014, the estimated fair value of the PIPE warrants was approximately $226,000 and $138,000, respectively, and is recorded as a liability on the Company's consolidated balance sheet. For the year ended

December 31, 2015, there was an increase of approximately $88,000 to the warrant liability, which was included in interest and other income (expense) on the consolidated statements of operations.

As of December 31, 2015 and 2014, the estimated fair value of the 2013 Sub-debt warrants was approximately $5,000 and $88,000, respectively, and is recorded as a liability on the Company's consolidated balance sheet. For the year ended December 31, 2015, there was a decrease of approximately $83,000 to the warrant liability, which was included in interest and other income (expense) on the consolidated statements of operations.

As of December 31, 2015, the estimated fair value of the 2015 Sub-debt warrants was approximately $672,000, and is recorded as a liability on the Company's consolidated balance sheet. Upon the refinance and issuance of 2015 Sub-debt warrants on April 6, 2015, the initial estimated fair value was $261,000. For the year ended December 31, 2015, there was an increase of approximately $411,000 to the warrant liability, which was included in interest and other income (expense) on the consolidated statements of operations.

The fair value was estimated using the Black-Scholes-Merton option pricing model, which requires the input of highly subjective assumptions as determined by management. To the extent these assumptions change in future periods, the fair value of the common stock warrants may increase or decrease and the change in fair value will be recorded in our results of operations. As of December 31, 2015 and December 31, 2014, all common stock warrants were outstanding.

3. Fair Value Measurements of Financial Instruments

The Company generally invests its excess cash in money market funds. Cash and cash equivalents represents highly liquid instruments with insignificant interest rate risk and original maturities of three months or less.

The Company has established a three-tier fair value hierarchy, categorizing the inputs used to measure fair value. The hierarchy can be described as follows: Level 1- observable inputs such as quoted prices in active markets; Level 2- inputs other than the quoted prices in active markets that are observable either directly or indirectly; and Level 3- unobservable inputs for which there is little or no market data, which require the reporting entity to develop its own assumptions.

Cash equivalents consist of money market funds that have original maturities of 90 days or less. These instruments are valued using quoted prices in active markets and are classified in Level 1 of the fair value hierarchy. At December 31, 2015, the fair value of the money market instruments was $1.9 million, accounted for at fair value on a recurring basis by level in accordance with the fair value hierarchy described above.

At December 31, 2015, the Company had no borrowings outstanding under its credit line with Bridge Bank. The line of credit is measured at the carrying value at each reporting period and is classified as a current liability, as loan payable. The line of credit is classified as a Level 1 in the Company's fair value hierarchy. The fair value of the line of credit approximates the carrying value.

The Company has no Level 2 financial assets or liabilities as of December 31, 2015 and 2014.

At December 31, 2015 the Company had outstanding warrants to purchase shares of its common stock, which were issued on March 28, 2012, April 5, 2013, and April 6, 2015. The warrants are measured at fair value each reporting period and are classified as liabilities with a combined fair value of $903,000 and $226,000 at December 31, 2015 and December 31, 2014, respectively. The warrants are valued using the Black-Scholes-Merton option pricing model using valuation assumptions determined by management and are classified as Level 3 in the Company's fair value hierarchy. To the extent these assumptions change in future periods, the fair value of the common stock warrants may increase or decrease and the change in fair value will be recorded in our results of operations.

The Company used the following assumptions when determining the fair value of the PIPE warrants:

	December 31,	
	2015	2014
Expected life (in years)	1.3	2.5
Risk-free interest rate	0.53 %	0.78 %
Dividend yield	0 %	0 %
Expected volatility	172 %	195 %

The Company assessed the sensitivity of the fair value of the PIPE warrants with respect to the assumptions above and noted that a change in the price of its common stock of 10% would affect the fair value of the warrants by 17% or approximately $38,000. A change in volatility of 10% would affect the fair value of the warrants by 23% or approximately $53,000.

The Company used the following assumptions when determining the fair value of the 2013 Sub-debt warrants:

	December 31,	
	2015	2014
Expected life (in years)	0.3	1.3
Risk-free interest rate	0.20 %	0.41 %
Dividend yield	0 %	0 %
Expected volatility	127 %	222 %

The Company assessed the sensitivity of the fair value of the 2013 Sub-debt warrants with respect to the assumptions above and noted that a change in the price of its common stock of 10% would affect the fair value of the warrants by 33% or approximately $1,800. A change in volatility of 10% would affect the fair value of the warrants by 67% or approximately $3,700.

The Company used the following assumptions when determining the fair value of the 2015 Sub-debt warrants:

	December 31, 2015	April 6, 2015
Expected life (in years)	4.3	5.0
Risk-free interest rate	1.59 %	1.31 %
Dividend yield	0 %	0 %
Expected volatility	100 %	100 %

The Company assessed the sensitivity of the fair value of the 2015 Sub-debt warrants with respect to the assumptions above and noted that a change in the price of its common stock of 10% would affect the fair value of the warrants by 11% or approximately $84,000. A sensitivity analysis of a change in volatility was not necessary for the 2015 Sub-debt warrants due to the fact that the warrant agreement fixed the volatility at 100%.

The following table summarizes the Company's financial liabilities as of December 31, 2015 and 2014, that are accounted for at fair value on a recurring basis by level in accordance with the fair value hierarchy described above, and the changes in fair value for the outstanding common stock warrants (*in thousands*):

	Change in FV of Common Stock Warrants
Balance at December 31, 2013	$ 495
Total change in fair value	(269)
Balance at December 31, 2014	$ 226
Issuance of warrants with subordinated debt financing	261
Total change in fair value	416
Balance at December 31, 2015	$ 903

The following is a summary of the Company's financial assets as of December 31, 2015 and 2014, that are accounted for at fair value on a recurring basis by level in accordance with the fair value hierarchy described above (*in thousands*):

	December 31, 2015			
	Level 1	Level 2	Level 3	Total
Assets:				
Money market instruments	$ 1,911	$ -	$ -	$ 1,911
Liabilities:				
Common stock warrants	$ -	$ -	$ 903	$ 903

	December 31, 2014			
	Level 1	Level 2	Level 3	Total
Assets:				
Money market instruments	$ 110	$ -	$ -	$ 110
Liabilities:				
Common stock warrants	$ -	$ -	$ 226	$ 226

4. Prepaid Expenses and Other Current Assets

Prepaid expenses and other current assets consist of the following (*in thousands*):

	December 31,	
	2015	2014
Prepaid expenses	$ 698	$ 744
Short-term deposit	18	100
Other receivables	5	66
Deferred rent	-	187
Total prepaid expenses and other current assets	$ 721	$ 1,097

5. Property and Equipment

Property and equipment consists of the following (*in thousands*):

	December 31,	
	2015	2014
Computer equipment and software	$ 7,843	$ 7,989
Office furniture and equipment	306	225
Leasehold improvements and leased equipment	1,017	1,022
Total property and equipment	9,166	9,236
Less: Accumulated depreciation	(8,499)	(8,771)
Total property and equipment, net	$ 667	$ 465

Depreciation and amortization expense for the years ended December 31, 2015 and 2014 was $0.3 million and $0.8 million, respectively.

6. Other Assets

Other assets consist of the following (*in thousands*):

	December 31,	
	2015	2014
Long-term lease deposits	$ 116	$ 16
Capitalized software, net	3	15
Other	37	2
Total other assets	$ 156	$ 33

7. Restructuring

As of December 31, 2015, $0.04 million of restructuring charges remains recorded within accrued liabilities on the consolidated balance sheets for restructurings activities that the Company performed during the years ended December 31, 2013 and 2012. These included a significant reduction in force in fiscal 2012 in the US and the closure of its Chinese operations in fiscal 2013. A significant portion of the remaining liability is related to severance payments for one officer that departed the Company in the third quarter of fiscal 2012, but is payable over an extended period of time.

Accrued costs are shown in the following table (*in thousands*):

	Restructuring
Accrued at December 31, 2013	$ 143
Cash payments	(42)
Adjustments	(14)
Accrued at December 31, 2014	$ 87
Cash payments	(49)
Accrued at December 31, 2015	$ 38

8. Warranties and Indemnification

The Company generally provides a warranty that the Company's software products substantially operate as described in the manuals and guides that accompany the software for a period of 90 days. The warranty does not apply in the event of misuse, accident, and certain other circumstances. To date, the Company has not incurred any material costs associated with these warranties and has no accrual for such items as of December 31, 2015 and 2014.

From time to time, the Company enters into contracts that require the Company, upon the occurrence of certain contingencies, to indemnify parties against third party claims. These contingent obligations primarily relate to (i) claims against the Company's customers for violation of third party intellectual property rights caused by the Company's products; (ii) claims resulting from personal injury or property damage resulting from the Company's activities or products; (iii) claims by the Company's office Lessor arising out of the use of the premises; and (iv) agreements with the Company's officers and directors under which the Company may be required to indemnify such persons for liabilities arising out of their activities on behalf of the Company. No liabilities have been recorded for these obligations as of December 31, 2015 and 2014.

9. Subordinated debt

On April 6, 2015, the Company re-financed its subordinated debt and issued $5.0 million of subordinated debt securities ("2015 sub-debt") and warrants to purchase an aggregate of 3,000,000 shares of the Company's common stock at an initial exercise price of $0.14 per share to a group of its current investors and one new investor. The new subordinated debt proceeds were used for the repayment of outstanding subordinated debt, working capital and general corporate purposes. The notes issued pursuant to the subordinated note and warrant purchase agreement bear simple interest at a rate of 12% per annum. The full principal is due on maturity on April 6, 2018 with the option of two one-year extensions. The Company will pay accrued interest in arrears on August 31 and November 30 and the final payment date. The Note and Warrant Purchase Agreement ("2015 Agreement") contains customary affirmative and negative covenants, including notification and information covenants and covenants restricting the Company's ability to merge or liquidate, incur debt, dispose of assets, incur liens, declare dividends or enter into transactions with affiliates. During the year ended December 31, 2015, the Company was in compliance with all covenants related to the subordinated debt. The 2015 Agreement also requires the Company to repay the notes upon the occurrence of a change of control (as defined in the 2015 Agreement) at 101% of the principal amount thereof plus accrued and unpaid interest.

The total value allocated to the 2015 sub-debt warrants was approximately $261,000 and was recorded as a debt discount against the proceeds of the notes and is being amortized to interest expense over term of the notes. See Note 2 to the consolidated financial statements. The aggregate debt issuance costs associated with the 2015 subordinated debt financing were $47,000 which are comprised of outside legal costs. These costs have been capitalized as debt issuance costs, and are being amortized as interest expense over the life of the notes. For the year ended December 31, 2015, the Company recorded interest expense related to the debt issuance costs of $12,000.

On April 5, 2013, the Company issued $4.6 million of subordinated debt securities ("2013 sub-debt") and warrants to purchase an aggregate of 1,846,940 shares of the Company's common stock, to a group of its current investors. The notes issued pursuant to the subordinated note and warrant purchase agreement bore simple interest at a rate of 12% per annum. From the issuance date through April 5, 2014, the Company accrued unpaid interest quarterly in arrears by increasing the principal amount of each note ("PIK Interest") and thereafter paid accrued interest in cash in arrears on July 31, 2014 and November 30, 2014. The notes matured on April 5, 2015. On April 6, 2015 the Company paid the outstanding balance of the 2013 sub-debt and the accrued interest in cash as part of the subordinated debt re-financing disclosed above.

The total value allocated to the 2013 sub-debt warrants was approximately $698,000 and was recorded as a debt discount against the proceeds of the notes and was amortized to interest expense over term of the notes. See Note 2 to the consolidated financial statements. The aggregate debt issuance costs associated with the 2013 subordinated debt financing were $118,000, which are comprised of outside legal costs. These costs were capitalized as debt issuance costs, and amortized as interest expense over the life of the notes. For the years ended December 31, 2015 and 2014 the Company recorded related interest expense related to the debt issuance costs of $15,000 and $59,000, respectively. This was fully amortized at December 31, 2015. As of December 31, 2014, the Company classified the subordinated debt in

long term liabilities, despite a maturity date of April 5, 2015. According to ASC 470-10-45, Intent and Ability to Refinance on a Long Term Basis, if a company intends to re-finance an obligation on a long-term basis and post-balance sheet date, but before that balance sheet issuance, and consummates a re-financing to a long term obligation, the short term obligation should be excluded from current liabilities. Due to the Company completing the re-financing of the subordinated debt as of April 6, 2015 the subordinated debt was classified as a long-term liability as of December 31, 2014.

At December 31, the Company's sub-debt notes payable is made up of the following (*in thousands*):

	December 31,	
	2015	2014
Subordinated notes payable	$ 5,000	$ 3,600
Deferred debt discount	(170)	(85)
Accrued PIK interest	-	577
Total subordinated debt	$ 4,830	$ 4,092

10. Loan payable

On June 23, 2014, the Company executed a Business Financing Agreement ("line of credit") with Bridge Bank. This agreement provides the Company a line of credit of $2 million secured by the Company's personal property and related assets. Advances on the line of credit are permitted up to 80% of eligible accounts receivable. The line of credit requires the Company to have a lock-box arrangement whereby customers are required to submit all payments on invoices to the lock-box. Bridge Bank controls the lock-box and all collections of financed receivables are used to pay off advances on the line of credit. The line of credit bears an interest rate of prime plus 3% per annum. The line of credit is a senior credit facility to the Subordinated Debt and terminates on April 5, 2015. Borrowings under the line of credit are subject to reporting covenants requiring the remittance of financial statements and supporting working capital reports to Bridge Bank.

On April 6, 2015, the Company extended the line of credit with Bridge Bank in conjunction with the refinance efforts as disclosed in Note 9 of the consolidated financial statements.

During the year ended December 31, 2015, the Company had a zero balance in borrowings under its line of credit and was in compliance with all financial reporting covenants.

11. Provision for Income Taxes

Substantially all income (loss) before income taxes is derived from the United States.

The components of the provision for income taxes are as follows (*in thousands*):

	Year Ended December 31,	
	2015	2014
Current:		
Federal	$ -	-
State	4	16
Foreign	-	-
Total current	$ 4	$ 16
Total provision for income taxes	$ 4	$ 16

Differences between income taxes calculated using the federal statutory income tax rate and the provision for income taxes were as follows (*in thousands*):

	Year Ended December 31,	
	2015	2014
Computed tax at statutory rate of 34%	$ (68)	$ 487
State taxes, net of federal benefit	-	8
Loss	14	32
Non deductible stock-based compensation	47	68
Fair value warrants	141	(91)
Other nondeductible expenses	17	35
Stock-based compensation write-offs	94	187
Net operating loss write-offs	38	342
Prior year trueups	(83)	36
Research & Development & Other Credits	(39)	-
Movement in valuation allowance	(157)	(1,088)
Provision for income taxes	$ 4	$ 16

Deferred income taxes reflect the net tax effects of temporary differences between carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Company's deferred tax assets (liabilities) are as follows (*in thousands*):

	Year Ended December 31,	
	2015	2014
Deferred tax assets:		
Net operating loss carryforwards	$ 30,596	$ 30,472
Deferred revenue	123	224
Research credit carryforwards	4,133	4,037
Intangibles (Excluding Goodwill)	1,130	1,284
Goodwill	800	906
Depreciable Assets	231	278
Other	419	388
Total gross deferred tax assets	37,432	37,589
Total gross deferred tax assets/liabilities	37,432	37,589
Valuation Allowance	(37,432)	(37,589)
Net deferred tax liability	$ -	$ -

As of December 31, 2015, the Company has U.S. federal and state net operating loss carryforwards of approximately $88.6 million and $31.9 million, respectively. The U.S. federal net operating loss carryforwards will expire at various dates beginning in 2019 through 2035 if not utilized. State net operating loss carryforwards will expire at various dates beginning in 2016 through 2035.

As of December 31, 2015, the Company has U.S. federal and state tax credit carryforwards of approximately $2.6 million and $3.8 million, respectively. The federal credit will expire at various dates beginning in 2018 through 2035, if not utilized. California state research and development credits can be carried forward indefinitely.

In connection with the Company's adoption of ASC 718, the Company uses the "with-and-without" approach described in EITF Topic No. D-32, "Intraperiod Tax Allocation of the Tax Effect of Pretax Income from Continuing Operations," to determine the recognition and measurement of excess tax benefits. In addition, the Company has elected to account for indirect effects of stock option based awards on other tax attributes, such as research and alternative minimum tax credits,

through the income statement. Accordingly, the Company has elected to recognize excess tax benefits from stock option exercises in additional paid in capital only if an incremental income tax benefit would be realized after considering all other tax attributes presently available to the Company.

Therefore, included in the net operating loss carryforwards are losses created by the exercise of stock options. Although these net operating loss carryforwards are reflected in total U.S. net operating tax loss carryforwards, pursuant to ASC 718, deferred tax assets associated with these deductions are only recognized to the extent that they reduce taxes payable. Further, these recognized deductions are treated as direct increases to stockholders' deficit and as a result do not impact the consolidated statement of operations. To the extent stock-option related deductions are not recognized pursuant to ASC 718, the unrecognized benefit is not reflected on the consolidated balance sheet.

Net operating loss carryforwards and credit carryforwards reflected above could be limited due to ownership changes as provided in the Internal Revenue Code and similar state provisions.

The Company does not provide for U.S. federal income and state income taxes on undistributed earnings of the China subsidiary at December 31, 2015 because these earnings are intended to be indefinitely reinvested. Upon distribution of those earnings in the form of dividends or otherwise, the Company would be subject to nominal U.S. federal and state income taxes.

The Company follows the provisions of FASB Interpretation ASC 740-10, “Accounting for Uncertainty in Income Taxes an interpretation of FASB ASC 740-10. ASC 740-10 prescribes a recognition threshold and a measurement attribute for the financial statement recognition and measurement of tax positions taken or expected to be taken in a tax return. For those benefits to be recognized, a tax position must be more-likely-than-not to be sustained upon examination by taxing authorities.

Interest and penalty costs related to unrecognized tax benefits are classified as a component of “Income tax expense” in the accompanying statement of operations and in "income taxes payable" or "prepaid income taxes" in the accompanying consolidated balance sheet. The Company recognized an immaterial amount of interest expense related to unrecognized tax benefits for the year ended December 31, 2015.

The Company files U.S. federal, state, and foreign income tax returns. Material jurisdictions are Federal and California tax returns, which remain open to examination by the appropriate governmental agencies for tax years 1997 to 2015. The federal and state taxing authorities may choose to audit tax returns for tax years beyond the statute of limitation period due to significant tax attribute carryforwards from prior years, making adjustments only to carryforward attributes. The Company is not currently under audit in any major tax jurisdiction.

A reconciliation of the beginning and ending amount of the consolidated liability for unrecognized income tax benefits during the twelve-month period ended December 31, 2015 is as follows (in thousands):

	Year Ended December 31,	
	2015	2014
Balance at December 31, 2014	$ 2,214	$ 2,193
Increases related to tax positions of current year	38	21
Balance at December 31, 2015	$ 2,252	$ 2,214

12. Stock-Based Compensation

Stock-Based Compensation Plans

On December 31, 2015, the Company had one active share-based compensation plan and one discontinued share-based compensation plan, which are described below.

In May 1999, the Company's stockholders approved the 1999 Equity Incentive Plan. The total number of shares authorized for issuance under the plan is 6,492,666. Restricted stock units awarded under this plan generally vest over four years of continuous service in annual or semi-annual installments. Option awards have generally been granted with an exercise price equal to the market price of the Company's common stock at the date of grant, and generally vest based on four years of continuous service with a ten-year contractual term.

In May 1999, the Company's stockholders approved the Employee Stock Purchase Plan (ESPP), which became effective upon the completion of the initial public offering of the Company's common stock. The total number of shares originally authorized for issuance under the plan was 700,000. In June 2007 and June 2011, an additional 500,000 shares were authorized, respectively. The total number of shares authorized for issuance under this plan is 1,700,000. At December 31, 2015, 137,850 shares were available for issuance under this plan. Effective June 1, 2014, the ESPP plan is inactive.

Stock-Based Compensation Expense

Compensation expense is recognized for the fair values of stock-based awards, which typically have graded vesting, on a straight-line basis over the requisite service period.

Forfeitures are required to be estimated at the time of grant. The estimates are revised in subsequent periods if actual forfeitures differ from those estimates. The Company uses historical data to estimate pre-vesting option forfeitures and records stock-based compensation expense only for those awards that are expected to vest. The following table summarizes the stock-based compensation expense recorded in the years ended December 31, 2015 and 2014 (*in thousands*):

	Year Ended December 31,	
	2015	2014
Cost of revenues	$ 1	$ 3
Sales and marketing	30	35
Research and development	4	22
General and administrative	203	290
Total stock-based compensation expense	$ 239	$ 350

Valuation of Stock Option Awards

The fair value of each option award is estimated on the date of grant using a Black-Scholes-Merton option pricing model with subjective assumptions, including expected stock price volatility, the expected life of each award and estimated pre-vesting forfeitures noted in the table below:

Expected volatility – Based on the historical prices of our common stock over the expected life of each option.

Expected life – Based on the history of option exercise and cancellation activity of the options.

Risk-free interest rate – Based on the U.S. Treasury yield curve in effect at the time of grants for periods corresponding with the expected life of the options.

Dividend yield – As the Company has not paid, nor does it currently plan to pay, dividends in the future, the assumed dividend yield is zero.

Estimated Forfeiture rate – Based on the history of option forfeitures and our expectations of future pre-vesting termination behavior.

The fair value of stock options granted was estimated using the following weighted-average assumptions:

	Year Ended December 31,	
	2015	2014
Expected life (in years)	3.7	4.8
Risk-free interest rate	1.1%	1.7%
Dividend yield	0%	0%
Expected volatility	174%	104%
Estimated forfeiture rate	16.4%	14.7%

Summary of Stock Options

The following table summarizes all stock option activity under the Company's stock-based compensation plans for the years ended December 31, 2015 and 2014:

	Number of Options	Weighted-Average Exercise Price Per Share	Weighted-Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value
Outstanding at December 31, 2013	2,051,300	$ 2.08	7.1	$ 2,980
Granted	18,750	0.24		
Forfeited	(11,793)	1.44		
Expired	(288,207)	4.61		
Outstanding at December 31, 2014	1,770,050	1.66	6.8	-
Outstanding at December 31, 2014	1,770,050	$ 1.66	6.8	
Granted	453,750	0.19		
Forfeited	(27,188)	0.53		
Expired	(176,212)	4.75		
Outstanding at December 31, 2015	2,020,400	1.10	6.6	$ 63,104
Vested and expected to vest at December 31, 2015	1,911,747	$ 1.15	6.5	$ 53,052
Exercisable at December 31, 2015	1,402,096	$ 1.39	5.8	$ 19,353

The aggregate intrinsic value of options outstanding at December 31, 2015 is calculated as the difference between the exercise price of the underlying options and the market price of the Company's common stock for shares that had exercise prices that were lower than the $0.28 market price of the Company's common stock at December 31, 2015 ("in the money options"). There were no options exercised during the year ended December 31, 2015. The fair value of options vested during the years ended December 31, 2015, and 2014 was $0.2 million and $0.2 million, respectively. The weighted average grant date fair value of options granted during the years ended December 31, 2015, and 2014 was $0.17 and $0.18 per share, respectively.

As of December 31, 2015, total unrecognized compensation cost related to stock options granted under the Company's various plans was $0.2 million. The Company expects that cost to be recognized over a weighted-average 2.3 years.

Summary of Restricted Stock Units and Restricted Stock Awards

The following table summarizes all restricted stock unit ("RSU") and restricted stock awards ("RSA") activity under the Company's stock-based compensation plans for the years ended December 31, 2015 and 2014:

	Number of Shares	Weighted-Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value
Outstanding at December 31, 2013	351,123	1.8	$ 82,549
Awarded	9,375		
Released (Vested)	(117,720)		
Forfeited	(6,250)		
Outstanding at December 31, 2014	236,528	1.6	$ 22,710
Awarded	209,375		
Released (Vested)	(282,565)		
Forfeited	(6,250)		
Outstanding at December 31, 2015	157,088	1.8	$ 43,356

The fair value of these RSUs and RSAs is calculated based upon the fair market value of the Company's stock at the date of grant, less an estimate of pre-vesting forfeitures. The weighted-average grant-date fair value of RSUs and RSAs awarded during fiscal years 2015 and 2014 was $0.12 and $0.24 per share, respectively, and the fair value of RSUs and RSAs that vested during fiscal years 2015 and 2014 was $0.1 million and $0.2 million, respectively. As of December 31, 2015, total unrecognized compensation cost related to restricted stock units was $0.1 million. The Company expects that cost to be recognized over a weighted-average 1.4 years.

Employee Stock Purchase Plan ("ESPP")

ESPP awards were valued using the Black-Scholes-Merton model using the following assumptions:

	Year Ended December 31,	
	2015	2014
Expected life (in years)	0.5 - 1.0	0.5 - 1.0
Risk-free interest rate	0.1%	0.1%
Dividend yield	0%	0%
Expected volatility	181%	181%

Disclosures Pertaining to All Share-Based Compensation Plans

Cash received under all share-based payment arrangements for the years ended December 31, 2015 and 2014 was zero and $0.01 million, respectively, related to the exercise of stock options and the purchase of ESPP shares. The Company discontinued the ESPP Plan in 2014. The Company issues new shares upon option exercise and does not repurchase or issue treasury shares.

13. Accrued Liabilities

Accrued liabilities consist of the following (*in thousands*):

	December 31,	
	2015	2014
Accrued vacation	$ 470	$ 466
Accrued commission and bonus	518	257
Accrued severance and retention	38	71
Other accrued liabilities	260	373
Accounts payable accruals	62	232
Total accrued liabilities	$ 1,348	$ 1,399

14. Deferred Revenue

Deferred revenue consists of the following (*in thousands*):

	December 31,	
	2015	2014
Current:		
Subscriptions	$ 3,845	$ 3,327
License	80	196
Service and support	3,907	4,350
Total deferred revenue, current portion	$ 7,832	$ 7,873
Long-term:		
Subscriptions	$ 50	$ 7
License	-	49
Service and support	174	307
Total deferred revenue, net of current portion	$ 224	$ 363

15. Commitments and Contingencies

On September 1, 2015, the Company entered into an agreement to lease approximately 7,226 square feet in Oakland, California for its new corporate headquarters. The term of the lease agreement is for 63 months from the lease commencement, which began in December 2015 and expires in March 2021. The Company also has a lease agreement for its Tucson, Arizona office, which was extended in June 2012 through August 2017. In addition, the Company leases certain equipment under capital lease arrangements that extend through 2019.

At December 31, 2015 the Company's future minimum lease payments are as follows (*in thousands*):

	2016	2017	2018	2019	2020 and thereafter	Total
Total	$ 456	$ 429	$ 282	$ 280	$ 315	$ 1,762

16. Common Stock

At December 31, 2015, the Company had reserved shares of common stock for future issuance as follows:

	2015
Stock options outstanding	2,020,400
Restricted stock awards/units outstanding	157,088
Stock options available for future grants	1,035,061
Employee stock purchase plan	137,850
Warrants	7,352,792
Total	10,703,191

17. Employee Retirement and Benefit Plan

The Company has a defined contribution retirement plan under Section 401(k) of the Internal Revenue Code, which covers substantially all employees. The Company did not match contributions by plan participants for the years ended December 31, 2015, and 2014.

18. Related Party Transactions

On December 20, 2013, the Company and Posit Science Corporation ("PSC") executed Amendment No. 3 to the SLC License Agreement, effective as of December 31, 2003. A co-founder, stockholder, and former member of the Board of Directors of the Company are a co-founder, officer, director and substantial stockholder of PSC. The original License Agreement granted PSC licenses in the Health Field (as defined in the License Agreement) to issued and pending patents held by the Company. PSC's licenses in the Health Field to many of the patents were exclusive. Under the Amendment, PSC agreed to make the exclusive licenses to 16 of the patents non-exclusive. PSC also agreed to amend the definition of Health Field as it applies to all non-exclusive licenses so as to reserve for the Company the field of Fitting of Hearing Aids and Cochlear Implants (as defined in the Amendment). In exchange for the changes in the license terms set forth in the Amendment, the Company agreed to a 90% reduction in PSC's annual minimum royalty payment of $150,000 and in the Applicable Base Royalty Percentage of New Sales set forth in the License Agreement. Accordingly, the annual minimum royalty payment is now $15,000 per year and the Applicable Base Royalty Percentage is now 0.4% of Net Sales. The Company has a 3.5% equity interest in PSC. The royalty income recorded from PSC was $0.015 million, for the years ended December 31, 2015 and 2014, respectively.

In July 2007, Michael A. Moses joined the Board of Directors as Vice Chair and entered into a consulting agreement with the Company. The consulting agreement originally provided for a consulting fee of $40,000 per year and two stock option grants, both with a five year term and at a per share exercise price of $7.15, the closing price of the Company's common stock on July 25, 2007. The first option grant for 80,000 shares vested over four years, with a one year cliff with ratable monthly vesting thereafter. The second option for 100,000 shares vests only in the event the per share price of the Company's common stock reaches and maintains for 20 consecutive business days a specified target closing price as follows: 25,000 shares vesting at each target stock price of $15, $20, $25, and $30. In January 2013, the Company revised the agreement with Dr. Moses to reduce his consulting fee to $36,000 per year. On April 1, 2013, in connection with the reduction in Dr. Moses' consulting fee, the Company issued Dr. Moses an additional grant of options for 40,000 shares with an exercise price of $0.7999 per share vesting in equal monthly installments over a three-year period commencing on April 1, 2013. The Company continues to renew the agreement with Dr. Moses and his consulting fee is $36,000 per year.

19. Interim Financial Information (unaudited)

Quarterly financial data (in thousands, except per share amounts):

	Three Months Ended				
	March 31	June 30	September 30	December 31	Total
Fiscal Year 2015:					
Total revenues	$ 3,852	$ 3,711	$ 5,826	$ 4,341	$ 17,730
Gross profit	$ 2,970	$ 2,900	$ 4,964	$ 3,408	14,242
Net income (loss)	$ (522)	$ (681)	$ 637	$ 361	$ (205)
Basic and diluted net income (loss) per share:	$ (0.02)	$ (0.03)	$ 0.03	$ 0.01	$ (0.01)
Fiscal Year 2014:					
Total revenues	$ 4,629	$ 5,183	$ 4,543	$ 4,816	$ 19,171
Gross profit	$ 3,540	$ 4,192	$ 3,567	$ 3,820	$ 15,119
Net income (loss)	$ 697	$ 656	$ (339)	$ 402	$ 1,416
Basic and diluted net income (loss) per share:	$ 0.03	$ 0.03	$ (0.01)	$ 0.01	$ 0.06

20. Subsequent Events

Management has evaluated subsequent events through March 3, 2016, the date the consolidated financial statements were available for issuance. No events have occurred that would have a material impact on the consolidated financial statements.

OTC Disclosures

Section 1: Name of Issuer

Scientific Learning Corporation

Section 2: Address of the issuer's principal executive offices

Company Headquarters
1956 Webster Street, Suite 200
Oakland, CA 94612-2943

888-665-9707
www.scilearn.com

IR Contact
No investor relations firm is currently engaged

Section 3: Security Information

Trading Symbol: **SCIL**
Exact title and class of securities outstanding: **Common Stock**
CUSIP: **808760102**

Par or Stated Value: **$0.001**
Total shares authorized: **40,000,000** as of: **12/31/2015**
Total shares outstanding: **24,344,001** as of: **12/31/2015**

Transfer Agent
Continental Stock Transfer & Trust Company
17 Battery Place
New York, NY 10004
212-509-4000

Is the Transfer Agent registered under the Exchange Act?* Yes: ☒ No: ☐

List any restrictions on the transfer of security:

None

Describe any trading suspension orders issued by the SEC in the past 12 months.

None

List any stock split, stock dividend, recapitalization, merger, acquisition, spin-off, or reorganization either currently anticipated or that occurred within the past 12 months:

None

Section 4: Issuance History

List below any events, in chronological order, that resulted in changes in total shares outstanding by the issuer in the past two fiscal years and any interim period. The list shall include all offerings of securities, whether private or public, and all shares or any other securities or options to acquire such securities issued for services, describing (1) the securities, (2) the persons or entities to whom such securities were issued and (3) the services provided by such persons or entities. The list shall indicate:

A. The nature of each offering (e.g., Securities Act Rule 504, intrastate, etc.)
B. Any jurisdictions where the offering was registered or qualified;
C. The number of shares offered;
D. The number of shares sold;
E. The price at which the shares were offered, and the amount actually paid to the issuer;
F. The trading status of the shares; and
G. Whether the certificates or other documents that evidence the shares contain a legend (1) stating that the shares have not been registered under the Securities Act and (2) setting forth or referring to the restrictions on transferability and sale of the shares under the Securities Act.

For history before January 1, 2015, please refer to the company's Annual Report for the fiscal year ended 2014, filed on and located at www.otcmarkets.com
The following table represents the Issuance History for the year ended December 31, 2015:

		A	B	C	D	E	E		F	G
Date	Entity	Nature of Offering	Juris.	Shares Offered	Shares Sold	Price Offered	Price Sold	Warrants	Trading Status	Legend
		Balance at December 31, 2014		**24,068,870**	**24,068,870**			**4,352,792**		
3/10/2015	Edward Vermont Blanchard, Jr	Director's RSU Vested	DE	939	939				Restricted	Rule 144
3/10/2015	Robert C. Bowen	Director's RSU Vested	DE	313	313				Restricted	Rule 144
3/10/2015	Rodman W. Moorhead III	Director's RSU Vested	DE	1,126	1,126				Restricted	Rule 144
3/10/2015	Michaeal A. Moses	Director's RSU Vested	DE	939	939				Restricted	Rule 144
3/10/2015	Paula A. Tallal	Director's RSU Vested	DE	939	939				Restricted	Rule 144
3/10/2015	Jeffrey D. Thomas	Director's RSU Vested	DE	939	939				Restricted	Rule 144
3/10/2015	Employees/Consultants	Employee's/Consultants RSU Vested	DE	12,500	12,500				Restricted	Rule 144
4/6/2015	Subordinated Debt Holders	Warrants issued with Subordinated Debt Offering	DE	-	-			**3,000,000**	Restricted	Rule 144
5/20/2015	Robert C. Bowen	Director's RSU Vested	DE	18,750	18,750				Restricted	Rule 144
5/20/2015	Employees/Consultants	Employee's/Consultants RSU Vested	DE	4,429	4,429				Restricted	Rule 144
7/1/2015	Edward Vermont Blanchard, Jr	Director's RSA Vested	DE	200,000	200,000				Restricted	Rule 144
9/10/2015	Edward Vermont Blanchard, Jr	Director's RSU Vested	DE	624	624				Restricted	Rule 144
9/10/2015	Employees/Consultants	Employee's/Consultants RSU Vested	DE	7,028	7,028				Restricted	Rule 144
9/10/2015	Rodman W. Moorhead III	Employee's/Consultants RSU Vested	DE	1,124	1,124				Restricted	Rule 144
9/10/2015	Michaeal A. Moses	Director's RSU Vested	DE	624	624				Restricted	Rule 144
9/10/2015	Paula A. Tallal	Director's RSU Vested	DE	624	624				Restricted	Rule 144
9/10/2015	Jeffrey D. Thomas	Director's RSU Vested	DE	624	624				Restricted	Rule 144
11/20/2015	Employees/Consultants	Director's RSU Vested	DE	4,859	4,859				Restricted	Rule 144
11/20/2015	Robert C. Bowen	Director's RSU Vested	DE	18,750	18,750				Restricted	Rule 144
		Balance at December 31, 2015		**24,344,001**	**24,344,001**			**7,352,792**		

Section 5: Financial Statements

See above

Section 6: Issuer's Business, Products and Services

A. Description of the issuer's business operations;

We are an education company that accelerates learning by applying proven research on how the brain learns in online and on premise software solutions. Our results show that learners who use our products can realize achievement gains of up to 2 years in as little as 3 months and maintain an accelerated rate of learning even after product use ends. We provide our learning solutions primarily to U.S. K-12 schools in traditional brick-and-mortar, virtual or blended learning settings and also to parents and learning centers, in approximately forty-five countries around the world.

We are highly differentiated because of our focus on the "science of learning" - combining advances in the field of brain research with standards-based learning objectives to achieve dramatic student gains. At December 31, 2013, proof that our products produce substantial academic gains was demonstrated in 282 efficacy studies, including randomized controlled trials and longitudinal studies, representing results from approximately 130,000 aggregate participants. These studies show gains for students at all K-12 grade levels, for at-risk, special education, English language, Title I (low income, under achieving), and a variety of other students. Gains have been demonstrated throughout the United States and in ten other countries. The studies show that these gains endure over time.

In 2011, we began implementing a software as a service (SaaS) model. Our easy-to-use and easy-to-access web-based platforms are able to effectively deliver individualized learning opportunities to a large number of students simultaneously. Our Fast ForWord and Reading Assistant educational software products are now available on our browser-based SciLEARN Enterprise software platform, which can be hosted on the customer's servers, and our on-demand platform MySciLEARN On Demand, which we host. The SciLEARN Enterprise and MySciLEARN platforms meet the needs of institution and district-wide installations by providing scalability, remote access, centralized reporting, asynchronous online professional development, and ease of administration for multiple campuses.

B. Date and State (or Jurisdiction) of Incorporation:

The Company was incorporated in 1995 in the State of California and was reincorporated in 1997 in the State of Delaware.

C. Issuer's primary and secondary SIC Codes:

Primary SIC Code: 73729903 Educational Computer Software
Secondary SIC Code: 8299, Schools and Educational Services

D. Issuer's fiscal year end date;

December 31, Calendar year

E. Principal products or services, and their markets;

Our principal products include: Fast ForWord, Fast ForWord Language and Literacy, Fast ForWord Reading, Reading Assistant, Results Now!, and BrainPro.

We sell to our principal market, K-12 schools and districts throughout the US and Canada, using a diversified direct sales channel, including both inside and field sales personnel. In addition to selling to K-12 schools, we also sell to and through private practice professionals and learning centers, international value-added resellers (VARs) and directly to consumers.

Section 7: Describe the Issuer's Facilities

We currently have the following leased properties:

1. **A lease for approximately 7,226 square feet of office space in Oakland, California for our new headquarters, which expires in March 2021.**

2. **A lease for approximately 10,800 square feet of office space in Tucson, Arizona for our sales and support center that expires in August 2017.**

Section 8: Officers, Directors, and Control Persons

Robert C. Bowen – Chairman and Chief Executive Officer
Edward V. Blanchard Jr. – Director
Christopher Brookhart - General Counsel, Secretary and Sr. Vice President
Rodman W. Moorhead III - Director
Michael A. Moses – Director
Steve Nathan - Vice President of Finance, Corporate Controller, and Treasurer
Paula A. Tallal - Director
Jeffrey D. Thomas - Director

B. Legal/Disciplinary History. Please identify whether any of the foregoing persons have, in the last five years, been the subject of:

1. A conviction in a criminal proceeding or named as a defendant in a pending criminal proceeding (excluding traffic violations and other minor offenses);

   None

2. The entry of an order, judgment, or decree, not subsequently reversed, suspended or vacated, by a court of competent jurisdiction that permanently or temporarily enjoined, barred, suspended or otherwise limited such person's involvement in any type of business, securities, commodities, or banking activities;

   None

3. A finding or judgment by a court of competent jurisdiction (in a civil action), the Securities and Exchange Commission, the Commodity Futures Trading Commission, or a state securities regulator of a violation of federal or state securities or commodities law, which finding or judgment has not been reversed, suspended, or vacated; or

   None

4. The entry of an order by a self-regulatory organization that permanently or temporarily barred suspended or otherwise limited such person's involvement in any type of business or securities activities.

   None

C. Beneficial Shareholders. Provide a list of the name, address and shareholdings or the percentage of shares owned by all persons beneficially owning more than ten percent (10%) of any class of the issuer's equity securities. If any of the beneficial shareholders are corporate shareholders, provide the name and address of the person(s) owning or controlling such corporate shareholders and the resident agents of the corporate shareholders.

Below is a list of Beneficial Owners as of December 31, 2015. This is most recent information that is available.

As of 12/31/2015	Shares Beneficially Owned (1)	
Beneficial Owner	**Number**	**Percent**
Nantahala Capital Management, LLC Daniel Mack 100 First Stamford Place, 2nd floor Stamford, CT 06902	7,393,857	30%

(1) This table is based upon information supplied by the shareholders. Applicable percentages are based on 24,344,001 shares outstanding on December 31, 2015.

Section 9: Third Party Providers

Below is the name, address, and telephone number of each of the following outside providers that advise the issuer on matters relating to operations, business development and disclosure

External Legal Counsel:
Wilson, Sonsini Goodrich & Rosati
650 Page Mill Road
Palo Alto, CA 94304
650.493.9300

Auditor:
Armanino LLP
12657 Alcosta Blvd.
Suite 500
San Ramon, CA 94583
925-790-2755

Investor Relations Consultant
No investor relations firm is currently engaged

Section 10: Issuer Certification

I, Robert C. Bowen certify that:

1. I have reviewed this annual disclosure statement of Scientific Learning Corporation for the year ended December 31, 2015 and December 31, 2014;

2. Based on my knowledge, this disclosure statement does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this disclosure statement; and

3. Based on my knowledge, the financial statements, and other financial information included or incorporated by reference in this disclosure statement, fairly present in all material respects the financial condition, results of operations and cash flows of the issuer as of, and for, the periods presented in this disclosure statement.

_____ March 3, 2016

_____ /s/Robert C. Bowen

_____ Chairman and Chief Executive Officer

I, Steve Nathan certify that:

1. I have reviewed this annual disclosure statement of Scientific Learning Corporation for the year ended December 31, 2015 and December 31, 2014;

2. Based on my knowledge, this disclosure statement does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this disclosure statement; and

3. Based on my knowledge, the financial statements, and other financial information included or incorporated by reference in this disclosure statement, fairly present in all material respects the financial condition, results of operations and cash flows of the issuer as of, and for, the periods presented in this disclosure statement.

_____ March 3, 2016

_____ /s/Steve Nathan

_____ Vice President of Finance, Corporate Controller and Treasurer