

AFFILIATED MANAGERS GROUP, INC.
 Form 4
 January 22, 2015

FORM 4

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

OMB APPROVAL

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Check this box if no longer subject to Section 16. Form 4 or Form 5 obligations may continue. See Instruction 1(b).

STATEMENT OF CHANGES IN BENEFICIAL OWNERSHIP OF SECURITIES

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

(Print or Type Responses)

1. Name and Address of Reporting Person *
 Dyson Andrew

2. Issuer Name and Ticker or Trading Symbol
 AFFILIATED MANAGERS GROUP, INC. [AMG]

5. Relationship of Reporting Person(s) to Issuer
 (Check all applicable)

(Last) (First) (Middle)
 C/O AFFILIATED MANAGERS GROUP, INC., 600 HALE STREET
 (Street)

3. Date of Earliest Transaction (Month/Day/Year)
 01/20/2015

____ Director _____ 10% Owner
 Officer (give title below) _____ Other (specify below)
 EVP(AMG Ltd.), Global Distrib.

PRIDES CROSSING, MA 01965

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

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

(City) (State) (Zip)

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

1. Title of Security (Instr. 3)	2. Transaction Date (Month/Day/Year)	2A. Deemed Execution Date, if any (Month/Day/Year)	3. Transaction Code (Instr. 8)	4. Securities Acquired (A) or Disposed of (D) (Instr. 3, 4 and 5)	5. Amount of Securities Beneficially Owned Reported Transaction(s) (Instr. 3 and 4)	6. Ownership Form: Direct (D) or Indirect (I) (Instr. 4)	7. Nature of Ownership (Instr. 4)
				(A) or (D)	Price		
				Code	V	Amount	

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

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SEC 1474 (9-02)

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

1. Title of Derivative	2. Conversion	3. Transaction Date (Month/Day/Year)	3A. Deemed Execution Date, if	4. Transaction	5. Number of Derivative	6. Date Exercisable and Expiration Date	7. Title and Amount of Underlying Securities	8. Pr
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Security (Instr. 3)	or Exercise Price of Derivative Security	any (Month/Day/Year)	Code (Instr. 8)	Securities Acquired (A) or Disposed of (D) (Instr. 3, 4, and 5)	(Month/Day/Year)	(Instr. 3 and 4)	Secu (Instr	
			Code V	(A) (D)	Date Exercisable	Expiration Date	Title	Amount or Number of Shares
Stock Units	(1)	01/20/2015	A	10,617	(1)	(1)	Common Stock	10,617

Reporting Owners

Reporting Owner Name / Address	Relationships			
	Director	10% Owner	Officer	Other
Dyson Andrew C/O AFFILIATED MANAGERS GROUP, INC. 600 HALE STREET PRIDES CROSSING, MA 01965				EVP(AMG Ltd.), Global Distrib.

Signatures

/s/ David M. Billings, Attorney-in-Fact
01/22/2015

**Signature of Reporting Person Date

Explanation of Responses:

- * If the form is filed by more than one reporting person, see Instruction 4(b)(v).
- ** Intentional misstatements or omissions of facts constitute Federal Criminal Violations. See 18 U.S.C. 1001 and 15 U.S.C. 78ff(a).
- (1) The award, issued under the Company's 2013 Incentive Stock Award Plan, vests in four equal installments on each of January 1, 2016, 2017, 2018, and 2019.

Note: File three copies of this Form, one of which must be manually signed. If space is insufficient, see Instruction 6 for procedure. Potential persons who are to respond to the collection of information contained in this form are not required to respond unless the form displays a currently valid OMB number. ISPLAY: inline">Mexico 274,182

	May 18, 2024	
China		200580015652.1
	May 18, 2024	
Canada		2,566,296
	May 18, 2024	
Japan		4790718
	May 18, 2024	
EPO (Validated in France, Germany and the United Kingdom)		2118935
	September 21, 2027	
Japan		

5175354

September 21, 2027

Australia

2005248343

May 18, 2024

South Korea

10-1497298

Trademarks

We have registered with the United States Patent and Trademark Office the trademark “Instant Connect” (Reg. No. 4,290,244 and 4,290,245) for the designation of our patented “plug and play” solar panel.

We have also registered the trademarks “Double Your Power” and “Andalay Solar” with the USPTO for two goods classes: providing computer software for photovoltaic systems for evaluating electric consumption, determining system sizing, estimating electrical output, estimating customer costs, and estimating financial life cycle savings, for use by consumers and businesses; and, installation of renewable energy systems, namely photovoltaic systems composed of solar panels, inverters, racks and electrical controls. Additionally, we have applications currently pending with the United States Patent and Trademark Office to expand the goods classes for “Double Your Power” and “Andalay Solar.”

From May 2010 until August 2013, we had been marketing our AC solar panels under the Westinghouse Solar brand, for which had licensed exclusive rights from Westinghouse Electric Corporation; however that license was terminated on August 23, 2013. We now market our products under the Andalay Solar brand.

Employees

As of July 17, 2015, we had 10 employees, of which 3 were sales and marketing employees, 3 were general and administrative employees, 3 were operations employees and 1 was a research and development employee. Seven employees were full-time employees and three were part-time. Our employees are not party to any collective bargaining agreement and we have never experienced an organized work stoppage. We believe our relations with our employees are good.

Property

Our principal executive offices and warehouse premises are located at 48900 Milmont Drive, Fremont, California 94538. On April 17, 2015, we entered into a sublease for 1,500 square feet of office space and 2,000 square feet of warehouse storage space for \$4,250 per month. The lease began when we initially occupied the new facilities on May 8, 2015 and the term will run for 12 months, expiring on May 30, 2016, after which it will be month-to-month.

We consolidated our executive offices with our warehouse premises effective January 1, 2014.

Legal Proceedings

On May 1, 2012, Suntech America, Inc., a Delaware corporation (Suntech America), filed a complaint for breach of contract, goods sold and delivered, account stated and open account against us in the Superior Court of the State of California, County of San Francisco. Suntech America alleged that it delivered products and did not receive full payment from us. On July 31, 2012, we and Suntech entered into a settlement of this dispute. Because of our inability to make scheduled settlement payments, on March 15, 2013, Suntech entered a judgment against us in the amount of \$946,438. As of March 7, 2014, Suntech has not sought to enforce its judgment. As of December 31, 2014 and 2013, we have included in our consolidated balance sheet a balance due to Suntech America of \$946,438.

In February 2015, the law firm of Snell & Wilmer LLP filed suit against us in California Superior Court, County of Orange. The complaint alleges that we have failed to pay Snell & Wilmer fees due to that firm in connection with prior patent prosecution litigation, in an amount of no less than \$808,202, plus interest. In June 2015, we entered into a settlement agreement with Snell whereby we agreed to pay \$250,000 in installments prior to an October 31, 2015 deadline. In the event that we do not pay all or part of the \$250,000 by such deadline, Snell may file a stipulation for entry of judgment for \$200,000 or \$250,000 plus interest with such amount depending upon what portion of the \$250,000 had been paid by Andalay prior to the deadline.

We are also involved in other litigation from time to time in the ordinary course of business. In the opinion of management, the outcome of such proceedings will not materially affect our financial position, results of operations or cash flows.

MARKET PRICE OF COMMON STOCK AND OTHER STOCKHOLDER MATTERS

As of July 20, 2015, our common stock began trading on the OTCQB. From May 15, 2015 through July 19, 2015, our common stock was quoted on the OTCPink. From September 6, 2012 to May 15, 2015, we trading on the OTCMKTS. From August 2010 to September 2012, we were traded on the NASDAQ Capital Market under the symbol WEST, from September 2007 until July 2010, we were traded under the symbol AKNS, and from August 2006 through August 2007, our common stock was quoted on the OTC Bulletin Board under the symbol AKNS.OB. Prior to that date, there was no active market for our common stock.

Our common stock is currently quoted on the OTCQB, which is sponsored by FINRA, which is a tier of the OTC Markets Group. The OTC Markets Group is a network of security dealers who buy and sell stock. The dealers are connected by a computer network that provides information on current “bids” and “asks,” as well as volume information. Our shares are quoted on the OTCQB under the symbol “WEST.”

The following table sets forth the range of high and low bid quotations for our common stock for each of the periods indicated as reported by the OTCQB/OTCPink. These quotations reflect inter-dealer prices, without retail mark-up, mark-down or commission and may not necessarily represent actual transactions.

Fiscal Year Ending December 31, 2015		
Quarter Ended	High \$	Low \$
June 30, 2015	\$0.02	\$0.01
March 31, 2015	\$0.02	\$0.01
Fiscal Year Ending December 31, 2014		
Quarter Ended	High \$	Low \$
December 31, 2014	\$0.02	\$0.01
September 30, 2014	\$0.03	\$0.01
June 30, 2014	\$0.04	\$0.02
March 31, 2014	\$0.05	\$0.02
Fiscal Year Ending December 31, 2013		
Quarter Ended	High \$	Low \$
December 31, 2013	\$0.05	\$0.02
September 30, 2013	\$0.05	\$0.02
June 30, 2013	\$0.06	\$0.02
March 31, 2013	\$0.13	\$0.03

Holders

The last reported sale price of our common stock on the OTCMKTS Marketplace on July 17, 2015, was \$0.01 per share. As of July 17, 2015, we estimate we had approximately 12,000 shareholders, of which 30 are record holders of our common stock.

Dividends

We have not declared or paid any cash dividends on our common stock and do not anticipate declaring or paying any cash dividends on our common stock in the foreseeable future. We currently expect to retain future earnings, if any, for the development of our business. Dividends may be paid on our common stock only if and when declared by our board of directors.

Penny Stock

Our stock is considered to be a penny stock. The SEC has adopted rules that regulate broker-dealer practices in connection with transactions in penny stocks. Penny stocks are generally equity securities with a market price of less than \$5.00, other than securities registered on certain national securities exchanges or quoted on the NASDAQ system, provided that current price and volume information with respect to transactions in such securities is provided by the exchange or system. The penny stock rules require a broker-dealer, prior to a transaction in a penny stock, to deliver a standardized risk disclosure document prepared by the SEC, that: (a) contains a description of the nature and level of risk in the market for penny stocks in both public offerings and secondary trading; (b) contains a description of the broker's or dealer's duties to the customer and of the rights and remedies available to the customer with respect to a violation of such duties or other requirements of the securities laws; (c) contains a brief, clear, narrative description of a dealer market, including bid and ask prices for penny stocks and the significance of the spread between the bid and ask price; (d) contains a toll-free telephone number for inquiries on disciplinary actions; (e) defines significant terms in the disclosure document or in the conduct of trading in penny stocks; and (f) contains such other information and is in such form, including language, type size and format, as the SEC shall require by rule or regulation.

The broker-dealer also must provide, prior to effecting any transaction in a penny stock, the customer with: (a) bid and offer quotations for the penny stock; (b) the compensation of the broker-dealer and its salesperson in the transaction; (c) the number of shares to which such bid and ask prices apply, or other comparable information relating to the depth and liquidity of the market for such stock; and (d) a monthly account statement showing the market value of each penny stock held in the customer's account.

In addition, the penny stock rules require that prior to a transaction in a penny stock not otherwise exempt from those rules, the broker-dealer must make a special written determination that the penny stock is a suitable investment for the purchaser and receive the purchaser's written acknowledgment of the receipt of a risk disclosure statement, a written agreement as to transactions involving penny stocks, and a signed and dated copy of a written suitability statement.

These disclosure requirements may have the effect of reducing the trading activity for our common stock. Therefore, stockholders may have difficulty selling our securities.

SECURITIES AUTHORIZED FOR ISSUANCE UNDER EQUITY COMPENSATION PLANS

Number of securities to be issued upon exercise of outstanding options	Weighted-average exercise price of outstanding options	Number of securities remaining available for issuance under equity compensation plans (excluding outstanding options and restricted stock awards)

Equity compensation plans approved by stock holders:				
2006 Stock Incentive Plan	37,034,483	\$	0.03	8,551,550
Equity compensation plans not approved by stock holders				
	—	\$	—	—

At our Annual Meeting of Stockholders held on June 9, 2015, our stockholders approved and adopted an amendment to our 2006 Incentive Stock Plan, increasing the number of shares of our common stock reserved for issuance under the Plan from 50,000,000 to 125,000,000.

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

Company Overview

We are a designer and manufacturer of integrated solar power systems and solar panels with integrated microinverters (which we call AC solar panels). We design, market and sell these solar power systems to solar installers and do-it-yourself customers in the United States, Canada, the Caribbean and South America through distribution partnerships, our dealer network and retail outlets. Our products are designed for use in solar power systems for residential and commercial rooftop customers. Prior to September 2010, we were also in the solar power installation business, but decided to exit that business. During the fourth quarter 2014, we re-entered the solar power installation business. Additionally, we are engaging in a new strategy of licensing our patented products to large module manufacturers and entering into distribution agreements with these manufacturers and large national distributors/installers. This new strategy is less capital intensive and aligns us with companies that have proven track records in the residential solar industry.

In September 2007, we introduced our “plug and play” solar panel technology (under the brand name “Andalay”), which we believe significantly reduces the installation time and costs, and provides superior reliability and aesthetics, when compared to other solar panel mounting products and technology. Our panel technology offers the following features: (i) mounts closer to the roof with less space in between panels; (ii) no unsightly racks underneath or beside panels; (iii) built-in wiring connections; (iv) approximately 70% fewer roof-assembled parts and approximately 50% less roof-top labor required; (v) approximately 25% fewer roof attachment points; (vi) complete compliance with the National Electric Code and UL wiring and grounding requirements. We have seven U.S. patents (Patent No. 7,406,800, Patent No. 7,832,157, Patent No. 7,866,098, Patent No. 7,987,641, Patent No. 8,505,248, Patent No. 8,813,460, and Patent No. 8,938,919) that cover key aspects of our Andalay solar panel technology, as well as U.S. Trademark No. 348565 3 for registration of the mark “Andalay Solar.” In addition to these U.S. patents, we have eight foreign patents. Currently, we have 15 issued patents and nine other pending U.S. and foreign patent applications that cover the Andalay technology working their way through the USPTO and foreign patent offices.

In February 2009, we began our strategic relationship with Enphase, a leading manufacturer of microinverters, to develop and market solar panel systems with ordinary AC house current output instead of high voltage DC output. We introduced Andalay AC panel products and began offering them to our customers in the second quarter of 2009. Andalay AC panels cost less to install, are safer, and generally provide higher energy output than ordinary DC panels. Andalay AC panels deliver 5-25% more energy compared to ordinary panels, produce safe household AC power, and have built-in panel level monitoring, racking, wiring, grounding and microinverters. With 80% fewer parts and 5 – 25% better performance than ordinary DC panels, we believe Andalay AC panels are an ideal solution for solar installers and do-it-yourself customers.

We are engaged in two business segments, (i) we market, sell, design and install systems for residential and commercial customers and (ii) we sell our AC solar panels to solar installers, trade workers and do-it-yourself customers through distribution partnerships, our dealer network and retail outlets. Operating segments are components of an enterprise for which separate financial information is available and is evaluated regularly by management in deciding how to allocate resources and in assessing performance.

In June 2015, we entered into a licensing agreement with Hyundai, whereby Hyundai will manufacture our frames under license from us. We have agreed to waive royalties under the agreement for a period of time in exchange for Hyundai investing resources to support this license agreement including as it relates to marketing, sales, certification and undertaking the needed modification of their manufacturing facility to produce the Andalay compatible modules. Hyundai has the right but not the obligation to produce Andalay compatible modules under the agreement. We believe

that having Hyundai available to produce the Andalay compatible modules will increase our addressable market given the bankability and name recognition of Hyundai among our target customers and intend to achieve and grow revenue by selling the mounting hardware that complements the Andalay compatible modules.

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Concentration of Risk

Supplier Relationships

We began receiving product from Tianwei in February 2014 and stopped as of June 2014. In July 2014, we entered into a supply agreement for assembly of our proprietary modules with Auxin Solar, Inc., a panel supplier located in the United States. We began receiving product from Auxin in December 2014. Although we believe we can find alternative suppliers for solar panels manufactured to our specifications, our operations would be disrupted unless we are able to rapidly secure alternative sources of supply, our inventory and revenue could diminish significantly, causing disruption to our operations.

Historically, we obtained virtually all of our solar panels from Suntech and Lightway. During 2012, because of our cash position and liquidity constraints, we were late in making payments to both of these suppliers. On March 30, 2012, pursuant to our Supply Agreement with Lightway, we issued 1,900,000 shares of our common stock to Lightway in partial payment of our past due account payable to them. At the time of issuance, the shares were valued at \$1,045,000. On May 1, 2012, Suntech filed a complaint for breach of contract, goods sold and delivered, account stated and open account against us in the Superior Court of the State of California, County of San Francisco. Suntech alleged that it delivered products and did not receive full payment from us. On July 31, 2012, we and Suntech entered into a settlement of this dispute. Because of our inability to make scheduled settlement payments, on March 15, 2013, Suntech entered a judgment against us in the amount of \$946,438. As of March 31, 2015, Suntech has not sought to enforce its judgment. As of March 31, 2015, we have included in accounts payable in our consolidated balance sheets a balance due to Suntech America of \$946,438. We currently have no unshipped orders from Suntech or Lightway.

Customer Relationships

The relative magnitude and the mix of revenue from our largest customers have varied significantly quarter to quarter. During the three months ended March 31, 2015, three customers have accounted for significant revenues, varying by period, to our company: Smart Energy Today (“Smart Energy”), which specializes in helping home owners and business owners become more energy efficient, Helco Electrics (“Helco”) a full-service provider of electrical services in southern Oregon, Verengo Solar (“Verengo”), a solar installer based in Southern California, Sustainable Environmental Enterprises (“SEE”), a leading provider of renewable energy and development projects located in New Orleans, Louisiana, and Shoreline Electric (“Shoreline”) a provider of residential and commercial electrical services in Southern California. For the three months ended March 31, 2015 and 2014, the percentages of sales of our top five customers are as follows:

	Three Months Ended March 31,			
	2015		2014	
Smart Energy Today	34.9	%	—	
Verengo Solar	13.9	%	22.9	%
Helco Electric	12.7	%	—	
Sustainable Environmental Enterprises	—		11.7	%
Shoreline Electric	—		31.9	%

During the year ended December 31, 2014, five customers have accounted for significant revenues, varying by period, to our company: Smart Energy Today (“Smart Energy”), which specializes in helping home owners and business owners become more energy efficient, WDC Solar, Inc. (“WDC”), a leading construction, integration and installation of commercial, residential and utility scale solar installations in the Washington D.C. area, JCF Wholesale (“JCF”) a provider of residential and commercial electrical services in Southern California, Lowe’s Companies, Inc. (Lowe’s), a nationwide home improvement retail chain, and Sustainable Environmental Enterprises (“SEE”), a leading provider of renewable energy and development projects located in New Orleans, Louisiana. For the year ended December 31, 2014 and 2013, the percentages of sales of our top five customers are as follows:

	Years Ended December 31,	
	2014	2013
Smart Energy Today	13.3%	13.5%
WDC Solar, Inc.	12.0%	14.7%
JCF Wholesale	8.7%	10.6%
Lowe’s	5.9%	6.9%
Sustainable Environmental Enterprises	1.3%	52.8%

The percentage of our gross accounts receivable for our top customers as of December 31, 2014 and 2013, are as follows:

	December 31,	
	2014	2013
WDC Solar, Inc.	40.1%	—
Lowe’s	16.8%	—
Sustainable Environmental Enterprises	—	86.7%
Smart Energy Today	6.5%	—

We maintain reserves for potential credit losses and such losses, in the aggregate, have generally not exceeded management’s estimates. Our top three vendors accounted for approximately 39% and 25% of purchases as of December 31, 2014 and 2013, respectively. As of December 31, 2014 and 2013, accounts payable included amounts owed to these top three suppliers of approximately \$0 and \$1.0 million, respectively.

The percentage of our gross accounts receivable for our top accounts receivable balance as of March 31, 2015 and December 31, 2014, are as follows:

	March 31, 2015	December 31, 2014
WDC Solar, Inc.	62.4%	40.1%
Lowe's Retail	11.6%	16.8%
Greg Teegarden	11.4%	—
Smart Energy	—	6.5%

We maintain reserves for potential credit losses and such losses, in the aggregate, have generally not exceeded management's estimates. Our top three vendors accounted for approximately 30% and 39% of purchases as of March 31, 2015 and December 31, 2014, respectively. As of March 31, 2015 and December 31, 2014, accounts payable included amounts owed to our top three suppliers of approximately \$68,000 and \$0, respectively.

Three Months Ended March 31, 2015 as Compared to Three Months Ended March 31, 2014

Results of Operations

The following table sets forth, for the periods indicated, certain information related to our operations, expressed in dollars and as a percentage of net revenue:

	Three Months Ended March 31,					
	2015			2014		
Net revenue	\$274,641	100.0	%	\$142,482	100.0	%
Cost of goods sold	286,382	104.3	%	135,388	95.0	%
Gross profit (loss)	(11,741)	(4.3)	%	7,094	5.0	%
Operating expenses						
Sales and marketing	71,129	25.9	%	63,384	44.5	%
General and administrative	721,358	262.7	%	604,164	424.0	%
Total operating expenses	792,487	288.1	%	667,548	468.5	%
Loss from continuing operations	(804,228)	(292.8)	%	(660,454)	(463.5)	%
Other income (expense)						
Interest expense, net	(62,213)	(22.7)	%	(77,085)	(54.1)	%
Adjustment to the fair value of embedded derivatives	41,265	15.0	%	(101,551)	71.3	%
Settlement of prior debt owed	—	0.0	%	769,148	539.8	%
Total other income (expense), net	(20,948)	(7.5)	%	590,512	414.4	%
Loss before provision for income taxes	(825,176)	(300.5)	%	(69,942)	(49.1)	%
Provision for income taxes	—	0.0	%	—	0.0	%
Net loss	(825,176)	(300.5)	%	(69,942)	(49.1)	%
Preferred stock dividend	—	(0.0)	%	(14,454)	(10.1)	%
Net loss attributable to common stockholders	\$(825,176)	(300.5)	%	\$(84,376)	(59.2)	%
Net loss attributable to common stockholders per common share (basic and diluted)	\$(0.00)			\$(0.00)		
Weighted-average shares used in computing loss per common share (basic and diluted)	327,997,747			131,428,001		

Net Revenue

We generate revenue from the sale and installation of solar power systems. For the three months ended March 31, 2015, we generated \$275,000 of revenue, an increase of \$133,000, or 92.8%, compared to \$142,000 of revenue for the three months ended March 31, 2014. The increase in revenue was due to an increase in watts sold, partially offset by a decrease in our average selling price per watt.

Cost of Goods Sold

Cost of goods sold as a percent of revenue for the three months ended March 31, 2015, was 104.3% of net revenue, compared to 95.0% for the three months ended March 31, 2014. Gross loss for the three months ended March 31, 2015, was \$12,000, or 4.3% of revenue, compared to gross profit of \$7,000 or 5.0% of revenue for the same period in 2014. The decrease in gross margin in the three months ended March 31, 2015, compared to the three months ended March 31, 2014, was due to higher inventory overhead allocations.

Explanation of Responses:

Sales and Marketing Expenses

Sales and marketing expenses for the three months ended March 31, 2015, were \$71,000, or 25.9% of net revenue as compared to \$63,000, or 44.5% of net revenue during the same period of the prior year. The \$8,000 increase in sales and marketing expenses for the three months ended March 31, 2015, compared to the same period in 2014 was primarily due to an increase of \$23,000 in payroll and commission expense, partially offset by a decrease of \$14,000 in travel and entertainment. The increase in payroll costs was due to higher headcount and an increase in commissions. The decrease in travel and entertainment was due to a decrease in travel costs.

General and Administrative Expenses

General and administrative expenses for the three months ended March 31, 2015, were \$721,000, or 262.7% of net revenue as compared to \$604,000, or 424.0% of net revenue during the same period of the prior year. The increase in general and administrative expense for the three months ended March 31, 2015, compared to the same period in 2014, was due primarily to an increase in payroll and benefits of \$79,000, professional fees of \$60,000, health insurance of \$25,000, accounting and legal fees of \$23,000 and settlement of \$20,000, partially offset by a decrease in stock compensation expense of \$105,000. The increase in payroll and benefits was due to higher headcount. The increase in professional fees was due to consulting fees. The increase in legal and accounting fees was due higher utilization of legal and accounting services. The decrease in stock compensation expense was due to the timing of restricted stock and stock option grants.

Interest Expense, Net

During the three months ended March 31, 2015, net interest expense was approximately \$62,000 compared with net interest expense of \$77,000 for the same period in 2014. The decrease in interest expense was associated with the decrease in the outstanding balance of notes payable and convertible debt.

Adjustment to the Fair Value of Embedded Derivatives

During the three months ended March 31, 2015, we recorded mark-to-market adjustments to reflect the fair value of embedded derivatives, resulting in an unrealized gain of approximately \$41,000 in our condensed consolidated statements of operations, compared to an unrealized loss of approximately \$102,000 for the same period in 2014.

Income Taxes

During the three months ended March 31, 2015 and 2014, there was no income tax expense or benefit for federal and state income taxes reflected in our condensed consolidated statements of operations due to our net loss and a valuation allowance on the resulting deferred tax asset.

Net Loss

Net loss from continuing operations for the three months ended March 31, 2015, was \$825,000, compared to a net loss from continuing operations of \$70,000 for the three months ended March 31, 2014.

Results of Operations

The following table sets forth, for the periods indicated, certain information related to our operations, expressed in dollars and as a percentage of net revenue:

	2014	%	2013	%
Net revenue	\$ 1,288,985	100.0	\$ 1,124,836	100.0
Cost of goods sold	1,191,390	92.4	1,121,612	99.7
Gross profit	97,595	7.6	3,224	0.3
Operating Expenses				
Sales and marketing	366,543	28.4	887,305	78.9
General and administrative	2,263,086	175.6	2,377,703	211.4
Total operating expenses	2,629,629	204.0	3,265,008	290.3
Loss from operations	(2,532,034)	(196.4)	(3,261,784)	(290.0)
Other Income (Expense)				
Interest income (expense), net	(362,955)	(28.2)	(65,031)	(5.8)
Adjustment to the fair value of embedded derivatives	(50,809)	(3.9)	65,962	5.9
Adjustment to the fair value of common stock warrants	—	0.0	9	0.0
Settlement of prior debt owed	769,148	59.7	420,000	37.3
Total other income, net	355,384	27.6	420,940	37.4
Loss before provision for income taxes	(2,176,650)	(168.9)	(2,840,844)	(252.6)
Provision for income taxes	—	—	—	—
Net loss from continuing operations	(2,176,650)	(168.9)	(2,840,844)	(252.6)
Gain from discontinued operations	324,349	25.2	10,797	1.0
Net loss	(1,852,301)	(143.7)	(2,830,047)	(251.6)
Preferred stock dividend	(18,927)	(1.5)	(153,305)	(13.6)
Preferred deemed dividend	—	0.0	(875,304)	(77.8)
Net loss attributable to common stockholders	\$ (1,871,228)	(145.2)	\$ (3,858,656)	(343.0)
Net loss per common and common equivalent share (basic and diluted) attributable to common shareholders				
	\$ (0.01)		\$ (0.06)	
Weighted average shares used in computing loss per common share: (basic and diluted)				
	203,814,897		69,170,957	

Year Ended December 31, 2014 as compared to Year Ended December 31, 2013

Net revenue

We generate revenue from the sale and installation of solar power systems. For the year ended December 31, 2014, we generated \$1.3 million of revenue, an increase of \$164,000, or 14.6%, compared to \$1.1 million of revenue for the year ended December 31, 2013. The increase in revenue was due to an increase in watts sold, partially offset by a decrease in our average selling price per watt.

Cost of goods sold

Cost of goods sold as a percent of revenue for the year ended December 31, 2014, was 92.4% of net revenue, compared to 99.7% for the year ended December 31, 2013. Gross profit for the year ended December 31, 2014 was \$98,000, or 7.6% of revenue, compared to gross profit of \$3,000 or 0.3% of revenue for the same period in 2013. The increase in gross profit in the year ended December 31, 2014 compared to the year ended December 31, 2013, was due to lower solar module costs and lower inventory overhead allocations due to increase in revenue.

Sales and marketing expenses

Sales and marketing expenses for the year ended December 31, 2014 were \$367,000, or 28.4% of net revenue as compared to \$887,000, or 78.9% of net revenue for the prior year. The \$521,000 decrease in sales and marketing expenses for the year ended December 31, 2014 compared to the same period in 2013 was primarily due to decreases in licensing fees owed to Westinghouse Electric Corporation of \$638,000, partially offset by an increase of \$78,000 in payroll and commission expense. The decrease in licensing fees was due to the termination of the licensing agreement with Westinghouse Electric. The increase in payroll costs was due to higher headcount.

General and administrative expenses

General and administrative expenses for the year ended December 31, 2014 were \$2.3 million, or 175.6% of net revenue, as compared to \$2.4 million, or 211.4% of net revenue during the same period of the prior year. The decrease in general and administrative expense for the year ended December 31, 2014 of \$115,000, or 4.8% of net revenue, compared to the same period in 2013, was due primarily to a decrease in rent expense of \$112,000, stock compensation expense of \$88,000, bad debt expense of \$55,000, insurance of \$66,000, research and development expense of \$65,000 and patent filing fees of \$14,000, partially offset by an increase in payroll and benefits of \$208,000 and professional fees of \$142,000. The decrease in stock compensation expense was due to the timing of restricted stock and stock option grants. The decrease in rent and insurance was due to the consolidation of our administrative offices with our warehouse. The decrease in patent filing fees was due to the filing of patents in the prior year. The increase in professional fees was primarily due legal and accounting consulting services. The increase in payroll and benefits expense was due to higher headcount.

Other Income, net

During the year ended December 31, 2014, other income was \$355,000 compared to \$421,000 for the year ended December 31, 2013. During the year ended December 31, 2014, we recorded a gain in other income of \$769,000 as a result of a favorable settlement on a prior debt owed to a creditor. During the year ended December 31, 2013, we recorded other income of \$420,000, net of legal fees, relating to the favorable settlement of a legal dispute relating to a supply agreement with a former customer.

Interest, net

During the year ended December 31, 2014, net interest expense was approximately \$363,000 compared with net interest expense of \$65,000 for the same period in 2013. The increase in interest expense was associated with the increase in notes payable and convertible debt.

Adjustment to the fair value of embedded derivatives

During the year ended December 31, 2014, we recorded mark-to-market adjustments to reflect the fair value of embedded derivatives, resulting in a loss of approximately \$51,000 in our consolidated statements of operations, compared to a gain of approximately \$66,000 for the prior year.

Adjustment to the fair value of common stock warrants

During the year ended December 31, 2013, the fair value of the warrants was reduced to zero as a result of the decrease in the price of our common stock.

Income taxes

During the year ended December 31, 2014 and 2013, there was no income tax expense or benefit for federal and state income taxes reflected in our consolidated statements of operations due to our net loss and a valuation allowance on the resulting deferred tax assets.

Net loss from continuing operations

Net loss from continuing operations for the year ended December 31, 2014 was \$2.2 million, compared to a net loss from continuing operations of \$2.8 million for the year ended December 31, 2013.

Gain from discontinued operations

During the year ended December 31, 2014, we recorded a \$324,000 gain from discontinued operations compared to a gain of \$11,000 in the prior year. During the year ended December 31, 2014, we re-evaluated our warranty liability related to our discontinued installation operations and in conjunction with re-entering the installation operations, we reduced the liability by approximately \$324,000.

Liquidity and Capital Resources

We currently face challenges meeting the working capital needs of our business. For the three months ended March 31, 2015 and for each of the two years in the period ended December 31, 2014, we have incurred net losses and negative cash flows from operations. During the recent years, we have undertaken several equity and debt financing transactions to provide the capital needed to sustain our business. We have dramatically reduced our headcount and other variable expenses. As of March 31, 2015, we had approximately \$135,000 of cash on hand. We intend to address ongoing working capital needs through sales of products, along with raising additional debt and equity financing. Our revenue levels remain difficult to predict, and we anticipate that we will continue to sustain losses in the near term, and we cannot assure investors that we will be successful in reaching break-even.

The accompanying consolidated financial statements have been prepared assuming we will continue as a going concern. Our significant operating losses, negative cash flow from operations, and challenges in rapidly securing alternative sources of supply for solar panels, raise substantial uncertainty about our ability to continue as a going concern. The accompanying consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty, and contemplate the realization of assets and the settlement of liabilities and commitments in the normal course of business. There can be no assurance that we will be able to raise additional funds on commercially reasonable terms, if at all. The current economic downturn adds uncertainty to our anticipated revenue levels and to the timing of cash receipts, which are needed to support our operations. It also worsens the market conditions for seeking equity and debt financing. As a result of our delisting from the Nasdaq Capital Market in September 2012, we are no longer eligible to file new registration statements on Form S-3, which may make it more costly and more difficult for us to obtain additional equity financing. We currently anticipate that we will retain all of our earnings, if any, for development of our business and do not anticipate paying any cash dividends on common stock in the foreseeable future.

Despite our recent financings, we have insufficient cash to operate our business at the current level for the next twelve months and insufficient cash to achieve our business goals. The success of our business plan is contingent upon us obtaining additional financing. We intend to fund operations through debt and/or equity financing arrangements such as the Equity Purchase Agreement with Southridge and the loan and security agreement discussed below; however there can be no assurance that we will meet the conditions necessary to be able to use the Equity Line under the Equity Purchase Agreement (described below) or the loan and security agreement (described below). Other than the

Equity Line and the loan and security agreement described below, we do not have any formal commitments or arrangements for the sales of stock or the advancement or loan of funds at this time. There can be no assurance that any additional financing will be available to us on acceptable terms, or at all. During the year ended December 31, 2014 and the first quarter of 2015, we funded a substantial portion of our cash needs through the sale of shares of our common stock under our prior equity line and under the December Equity Purchase Agreement. During the year ended December 31, 2014, we received approximately \$883,000 from the sale of shares of our common stock under our prior equity line and through July 17, 2015, we have received approximately \$1,105,000 from the sale of shares under the December Equity Purchase Agreement.

On January 22, 2014, we entered into a Settlement of Potential Claims Agreement (the "ASC Agreement") with ASC Recap LLC ("ASC"), an entity affiliated with Southridge. Pursuant to the ASC Agreement, ASC has offered to purchase (and in one (1) case has already purchased) approximately \$3.7 million of our prior debt owed to four creditors ("Creditors") for past due services at a substantial discount to face value to which we have agreed to issue to ASC certain shares of our common stock in a §3(a)(10) 1933 Act proceeding. The shares of common stock that we have agreed to issue to ASC in full payment for, and as a release of any debt it purchases from the Creditors, is anticipated to have, upon issuance, a market value equal to approximately 25% of the principal amount of our outstanding debt. In the case of the debt ASC already purchased from one (1) Creditor, we entered into a Settlement Agreement and Stipulation that was filed with the Circuit Court of the Second Judicial Circuit, Leon County, Florida pursuant to which we agreed, subject to court approval, to issue shares of our common stock that generate proceeds in the amount of \$250,000 in full settlement of a claim in the amount of \$1,027,705 that ASC Recap acquired from one Creditor (the value of the stock that we agreed to issue was two hundred and fifty percent (250%) of the discounted purchase price ASC paid to purchase the debt from the Creditor, and approximately 25% of the original amount we owed to the Creditor). The court subsequently approved the settlement and 8,079,800 shares were issued,

Convertible Notes payable

On August 30, 2013, we entered into a securities purchase agreement with Alpha Capital Anstalt ("Alpha Capital") relating to the sale and issuance of a convertible note in the principal amount of \$200,000 that matures August 29, 2015 (the "Convertible Note"). Subsequently, on November 25, 2013 and December 19, 2013, we entered into additional securities purchase agreements with Alpha Capital relating to the sale and issuance of convertible notes in the principal amount of \$200,000 and \$250,000, respectively, which mature on November 25, 2015 and December 19, 2015. On January 27, 2014, we issued a convertible note in the principal amount of \$100,000 that matures January 27, 2016 under the Securities Purchase Agreement we entered into with Alpha Capital on December 19, 2013. In connection with the issuance of the December 19, 2013 convertible note, we also issued 6,250,000 warrants to purchase shares of our common stock at a price of \$0.02 per share. On February 25, 2014, we entered into a Securities Purchase Agreement with the Alpha Capital related to the sale and issuance of a convertible note in the principal amount of \$200,000 that matures February 25, 2016. In connection with the issuance of the February 25, 2014 convertible note, we issued 5,000,000 warrants to purchase shares of our common stock at a price of \$0.02 per share. On March 18, 2014, we entered into a Securities Purchase Agreement we entered into with the Alpha Capital related to the sale and issuance of a convertible note in the principal amount of \$300,000 that matures March 18, 2016. In connection with the March 18, 2014 convertible note, we issued a five-year warrant to purchase 7,500,000 shares of our common stock at an exercise price of \$.02 per share. Each of the Convertible Notes bear interest at the rate of 8% per annum compounded annually, are payable at maturity and the principal and interest outstanding under the convertible notes are convertible into shares of our common stock, at any time after issuance, at the option of the purchaser, at a conversion price equal to \$0.02 per share, subject to adjustment upon the happening of certain events, including stock dividends, stock splits and the issuance of common stock equivalents at a price below the conversion price. Subject to our fulfilling certain conditions, including beneficial ownership limits, the convertible notes are subject to a mandatory conversion if the closing price of our common stock for any 20 consecutive days commencing six months after the issue date of the convertible notes equal or exceeds \$0.04 per share. Unless waived in writing by the purchaser, no conversion of the convertible notes can be effected to the extent that as a result of such conversion the purchaser would beneficially own more than 9.99% in the aggregate of our issued and outstanding common stock immediately after giving effect to the issuance of common stock upon conversion.

We have the option of repaying the outstanding principal amount of the convertible notes, in whole or in part, by paying the purchaser a sum of money equal to one hundred and twenty percent (120%) of the principal together with accrued but unpaid interest upon 30 days' notice, subject to certain beneficial ownership limits. For so long as we have any obligation under the convertible notes, we have agreed to certain restrictions regarding, among other things, incurrence of additional debt, liens, amendments to charter documents, repurchase of stock, payment of cash

dividends, affiliated transactions. We are also prohibited from entering into certain variable priced agreements until the convertible notes are repaid in full, except for the Equity Line we have with Southridge.

Because of certain down-round protection in the conversion rate of the convertible notes, we determined that the derivative liability related to the embedded conversion feature met the criteria for bifurcation. Accordingly, we recognized an aggregate liability of \$123,000 on the three issuance dates during the year ended December 31, 2014. This was in addition to the carrying value of the derivative liability on three previously recorded derivatives of \$178,000. The derivative liability is carried at fair value with changes in the fair value reflected in the "Adjustment to the fair value of embedded derivatives" line item of our condensed consolidated statements of operations. We recognized a loss for the year ended December 31, 2014 of \$51,000 on our convertible notes.

The relative fair value of the warrants issued in the December 2013 convertible note issuance of \$250,000, were allocated to additional paid-in capital. Such value was determined assuming volatility of 149.1%, a risk free interest rate of 0.7% and an expected term of 4.1 years. The resulting debt discount from the derivative liability and warrant issuance of \$109,000 is being accreted to interest using the effective interest method. The relative fair value of the warrants issued in the February 2014 convertible note issuance of \$200,000, were allocated to additional paid-in capital. Such value was determined assuming volatility of 169.1, a risk free interest rate of 0.7% and an expected term of 4.1 years. The resulting debt discount from the derivative liability and warrant issuance of \$101,000 is being accreted to interest using the effective interest method. The relative fair value of the warrants issued in the March 2014 convertible note issuance of \$300,000, were allocated to additional paid-in capital. Such value was determined assuming volatility of 168.8%, a risk free interest rate of 0.8% and an expected term of 4.1 years. The resulting debt discount from the derivative liability and warrant issuance of \$154,000 is being accreted to interest using the effective interest method.

On November 1 and December 1, 2013, and on January 1, February 1 and March 1, 2014, we issued convertible notes to our financial advisory firm in the principal amount of \$30,000 each for a total of \$150,000, which mature on October 31, November 30 and December 31, 2014, and on January 31 and February 28, 2015, respectively. On April 1, May 1 and June 1, 2014, we issued convertible notes to our financial advisory firm in the principal amount of \$20,000 each, for a total of \$60,000, which mature on March 31, April 30 and May 31, 2015, respectively. On July 1, 2014, we issued convertible notes to our financial advisory firm in the principal amount of \$10,000, which matures on June 30, 2015. Each of the Convertible Notes bear interest at the rate of 8% per annum compounded annually, are payable at maturity and the principal and interest outstanding under the convertible notes are convertible into shares of our common stock, at any time after issuance, at the option of the purchaser, at a conversion price equal to \$0.02 per share. Unless waived in writing by the purchaser, no conversion of the convertible notes can be effected to the extent that as a result of such conversion the purchaser would beneficially own more than 9.99% in the aggregate of our issued and outstanding common stock immediately after giving effect to the issuance of common stock upon conversion. As of December 31, 2014, convertible notes in the principal amount of \$940,000, along with accrued interest of \$68,319, were converted into 50,439,751 shares of our common stock.

Line of credit

On September 30, 2013, we entered into a loan and security agreement with Alpha Capital Anstalt and Collateral Services, LLC to provide financing, on a discretionary basis, for one year, against our accounts receivable and inventory. The maximum amount that can be borrowed under the Agreement is \$500,000. We have the right to borrow up to 80% of our eligible accounts receivable, not in excess of \$200,000, 50% of the value of our raw materials in inventory, 65% of our finished goods inventory and 95% of cash, but not in the aggregate amount in excess of \$300,000. The advances are secured by a lien on all of our assets. All advances under the agreement bear interest at a per annum rate of 12% and monthly interest shall be a minimum of \$500. At the time of initial funding we paid a loan fee of 50 shares of our Series D Preferred Shares to the lender, in addition to other payments for legal fees. In addition, we paid the collateral agent an initial fee of \$5,000 and have agreed to pay an administrative fee to the collateral agent of 0.5% per month of the daily balance during the preceding month or \$500 whichever is less. In the event that of a prepayment, we are obligated to pay a prepayment fee in an amount equal to one-half of one percent (0.5%) of \$500,000. On September 30, 2013, we requested and received an initial borrowing under the Agreement totaling \$350,000. Subsequently, on October 21, 2013, we requested and received an additional \$100,000 and on November 20, 2013, we requested and received an additional \$50,000. As of December 31, 2014, the balance outstanding under our line of credit was \$500,000. On February 27, 2015, we agreed to extend the term of the agreement for one year, and to exchange the \$500,000 plus interest owing under the agreement for a one year, 8%, convertible note. We are no longer able to make borrowings under the agreement. The convertible note is convertible at \$0.01 per share of common stock.

On the date we issued the convertible note to Alpha Capital, our stock price was \$0.0155 per share of common stock. As a result of the difference between the stock price at the time of issuance and the conversion price, we recorded a beneficial conversion feature in the amount of \$275,000 as a reduction to the Convertible Note and an increase in additional paid-in capital on our condensed consolidated balance sheets. The beneficial conversion feature is being amortized over the 12 month term of the Note. We recorded additional interest expense of approximately \$23,000 during the quarter ended March 31, 2015 related to the beneficial conversion feature.

Equity Purchase Agreement

On December 10, 2014, we entered into the December Equity Purchase Agreement) with Southridge, that superseded our prior Equity Purchase Agreement with Southridge that was entered into on January 23, 2014 (the “Prior Equity Purchase Agreement”). The terms of the December Equity Purchase Agreement are substantially similar to those of the Prior Equity Purchase Agreement.

Pursuant to the December Equity Purchase Agreement and as provided in the Prior Equity Purchase Agreement, Southridge has committed to purchase up to \$5,000,000 worth of our common stock, over a period of time terminating on the earlier of: (i) July 16, 2016, which is 18 months from the effective date of the Initial Registration Statement; or (ii) the date on which Southridge has purchased an aggregate maximum purchase price of \$5,000,000 pursuant to the December Equity Purchase Agreement; Southridge’s commitment to purchase our common stock is subject to various conditions, including, but not limited to, limitations based on the trading volume of our common stock. During the year ended December 31, 2014 and the first quarter of 2015, we funded a substantial portion of our cash needs through the sale of shares of our common stock under our prior equity line and under the December Equity Purchase Agreement. During the year ended December 31, 2014, we received approximately \$883,000 from the sale of shares of our common stock under our prior equity line and through July 17, 2015, we have received approximately \$1,105,000 from the sale of shares under the December Equity Purchase Agreement.

We intend to draw on the facility from time to time, as and when we determine appropriate in accordance with the terms and conditions of the December Equity Purchase Agreement. The purchase price for our shares to be paid by Southridge will be 90% of the volume weighted average price (total dollar value traded for all transactions (share price multiplied by number of shares traded) divided by the total quantity of shares traded for the day) on the principal market for each of the trading days of our common stock during the ten (10) trading days immediately following the clearing date. On the date the Draw Down Notice is delivered to Southridge, we are required to deliver an estimated amount of shares to Southridge’s brokerage account equal to 125% of the Draw Down Amount indicated in the Draw Down Notice divided by the closing bid price of the trading day immediately prior to the date of the Draw Down Notice (“Estimated Shares”). The Valuation Period will begin the first trading day after the Estimated Shares have been delivered to Southridge’s brokerage account and have been cleared for trading and terminates on the tenth day thereafter. At the end of the Valuation Period, if the number of Estimated Shares delivered to Southridge is greater than the shares issuable pursuant to a Draw Down, then Southridge is required to return to us the difference between the Estimated Shares and the actual number of shares issuable pursuant to the Draw Down. If the number of Estimated Shares is less the shares issuable under the Draw Down, then we are required to issue additional shares to Southridge equal to the difference; provided that the number of shares to be purchased by Southridge may not exceed the number of shares that, when added to the number of shares of our common stock then beneficially owned by Southridge, would exceed 9.99% of our shares of common stock outstanding. As a result, our existing shareholders will experience immediate dilution upon the purchase of any of the shares by Southridge. If we fail to satisfy the applicable closing conditions, we will not be able to sell the put shares to Southridge.

There are put restrictions applied on days between the put notice date and the closing date with respect to that particular put. During such time, we are not entitled to deliver another put notice.

The conditions under which we will not be entitled to put shares to Southridge, including the following:

we will not be entitled to put shares to Southridge unless there is an effective registration statement under the Securities Act of 1933, as amended (the “Securities Act”), to cover the resale of the shares by Southridge;

we will not be entitled to put shares to Southridge unless our common stock continues to be publicly traded;

we will not be entitled to put shares to Southridge if an injunction shall have been issued and remain in force against us, or action commenced by a governmental authority which has not been stayed or abandoned, prohibiting the purchase or the issuance of the shares to Southridge;

we will not be entitled to put shares to Southridge if we have not complied with our obligations and are otherwise in breach of or in default under, the Equity Purchase Agreement, our registration rights agreement with Southridge (the "Registration Rights Agreement") or any other agreement executed in connection therewith with Southridge;

we will not be entitled to put shares to Southridge to the extent that such shares would cause Southridge's beneficial ownership to exceed 9.99% of our outstanding shares; and

we will not be entitled to put shares to Southridge if we take any of the following actions on any trading day after a Draw Down Notice is delivered:

- a) subdivide or combine shares of common stock;
- b) pay a dividend in shares of common stock or make any other distribution of shares of common stock, except for dividends paid with respect to any series of preferred stock authorized by us, whether existing now or in the future;
- c) issue any options or other rights to subscribe for or purchase shares of common stock other than pursuant to the Equity Purchase Agreement, and other than options or stock grants issued or issuable to directors, officers and employees pursuant to a stock option program, whereby the price per share for which shares of common stock may at any time thereafter be issuable pursuant to such options or other rights shall be less than the closing bid price in effect immediately prior to such issuance;
- d) issue any securities convertible into or exchangeable for shares of common stock and the consideration per share for which shares of common stock may at any time thereafter be issuable pursuant to the terms of such convertible or exchangeable securities shall be less than the closing bid price in effect immediately prior to such issuance;
- e) issue shares of common stock otherwise than as provided in the foregoing subsections (a) through (d), at a price per share less, or for other consideration lower, than the closing bid price in effect immediately prior to such issuance, or without consideration; or
- f) make a distribution of our assets or evidences of indebtedness to the holders of common stock as a dividend in liquidation or by way of return of capital or other than as a dividend payable out of earnings or surplus legally available for dividends under applicable law or any distribution to such holders made in respect of the sale of all or substantially all of our assets (other than under the circumstances provided for in the foregoing subsections (a) through (e)).

The December Equity Purchase Agreement further provides that Southridge is entitled to customary indemnification from us for any losses or liabilities it suffers as a result of any material misrepresentation, breach of warranty or nonfulfillment of or a failure to perform any material covenant or agreement contained in the December Equity Purchase Agreement.

The December Equity Purchase Agreement also contains representations and warranties of each of the parties.

Pursuant to the terms of the December Equity Purchase Agreement paid Southridge a commitment fee of 1 million shares of our common stock (having a value of \$17,900 based upon the closing price of our common stock on December 5, 2014), of which 500,000 shares of our common stock were issued to Southridge on the date that the registration statement was declared effective, January 16, 2015, and the remaining 500,000 shares of common stock were issued on the date that we delivered our first Draw Down Notice to Southridge.

On December 10, 2014, we also entered into a Registration Rights Agreement with Southridge pursuant to which we registered shares of the common stock to be issued to Southridge in connection with the December Equity Purchase Agreement.

We submitted various take-down requests during the first quarter and second quarter of 2015 pursuant to the terms of the December Equity Purchase Agreement. As of July 17, 2015, 84,113,042 shares had been sold at an average price of \$0.0132 per share, resulting in total proceeds of approximately \$1,105,000.

Equity Financing Activity

Explanation of Responses:

On October 18, 2012, we entered into a securities purchase agreement with certain institutional accredited investors relating to the sale and issuance of up to 1,245 shares of our newly created Series C 8% Convertible Preferred Stock at a price of \$1,000 per share, for aggregate proceeds of up to \$1,245,000. At the initial closing, we sold and issued 750 shares of Series C Preferred, for initial aggregate proceeds of \$750,000. Subsequently, on November 2, 2012, we sold and issued 350 shares of Series C Preferred for proceeds of \$350,000. On January 24, 2013, we provided to the purchasers of our Series C Preferred Stock a draw down notice under the purchase agreement. The purchasers agreed to accept the new draw down notice and thereby extend our right to exercise a “put” to sell additional Series C Preferred beyond the securities purchase agreement’s prior expiration date of December 31, 2012. As a result of the draw down, we sold an aggregate of 75 additional shares of Series C Preferred to the purchasers for aggregate proceeds of \$75,000. Based on the closing price of our common stock as reported on the OTCQB Marketplace on January 24, 2013 (which was \$0.05 per share), the 75 shares of Series C Preferred to be issued pursuant to the draw down would be convertible into 1,500,000 shares of our common stock. As a result of the contingent conversion feature on the Series C Preferred, which reduced the conversion price from \$0.08 to \$0.05 per share on the total 720 shares of Series C Preferred Stock issued and outstanding at January 24, 2013, and which resulted in an increase in the number of common shares issuable, we recognized additional preferred deemed dividends of \$270,000.

As a result of the January 24, 2013 draw down notice, pursuant to the terms of the outstanding Series B Preferred Stock, the conversion price of the Series B Preferred was reduced from \$0.08 per share of common stock to become equal to \$0.05, and the conversion price of the Series C Preferred issued under the initial closing was reduced from \$0.08 per share of common stock to become equal to \$0.05. As a result of the May 13, 2013 draw down notice, the price of the Series B Preferred was further reduced from \$0.05 per share of common stock to become equal to \$0.03, and the conversion price of the Series C Preferred was also further reduced from \$0.05 per share of common stock to \$0.03. As of December 31, 2013, there were 467 shares of Series B Preferred that remain outstanding. With the May 13, 2013 draw down, and after recent conversions of our Series C Preferred, there are 87 shares of Series C Preferred that remain outstanding. As a result of our August 30, 2013 financing, the conversion price of the Series B Preferred was further reduced from \$0.03 per share of common stock to \$0.02 and the conversion price of the Series C Preferred was also further reduced from \$0.03 per share of common stock to \$0.02.

On February 15, 2013, we entered into a securities purchase agreement with an institutional accredited investor relating to the sale and issuance of up to 1,180 shares of our newly created Series D Preferred Stock at a price per share equal to the stated value, which is \$1,000 per share, for aggregate proceeds of up to \$1,000,000. At the initial closing, concurrent with entering the agreement, we issued 150 shares of Series D Preferred, for initial aggregate proceeds of \$150,000. After the initial closing, the securities purchase agreement permits the purchaser to exercise a "call" right to purchase additional Series D Preferred in multiple draw downs from time to time until December 31, 2013, subject to certain limits, terms and conditions. In March 2013, we and certain investors entered into a letter agreement to the securities purchase agreement dated as of February 15, 2013, modifying the number of shares of Series D Preferred Stock to be issued upon settlement of any purchaser draw downs made on or after March 18, 2013, equal to the purchaser investment amount divided by the stated value multiplied by a number agreed upon by the Company and the purchaser, which shall not be higher than 1.67. Subsequently, on March 21, 2013, we issued 167 shares of Series D Preferred for aggregate proceeds of \$100,000. On May 13, 2013, we entered into a letter agreement amendment to the securities purchase agreement dated as of February 15, 2013 with certain investors, modifying the number of shares of Series D Preferred Stock that may be issued upon draw downs made on or after May 13, 2013, equal to the purchaser investment amount divided by the stated value multiplied by a number agreed upon by us and the purchaser, which shall not be higher than 3.34. The corresponding conversion price into underlying shares of our common stock is \$0.03 per share. On May 13, 2013, we issued 583 shares of Series D Preferred to an investor for aggregate proceeds of \$175,000. As a result of the contingent conversion feature on the Series C Preferred, which reduced the conversion price from \$0.05 to \$0.03 per share on the total 260 shares of Series C Preferred Stock issued and outstanding at May 13, 2013, and which resulted in an increase in the number of common shares issuable, we recognized additional preferred deemed dividends of \$104,000. On August 30, 2013, we entered into an agreement to sell \$200,000 in convertible notes. As a result of the sale of these convertible notes and as a result of the contingent conversion feature on the Series C Preferred and Series D Preferred, which reduced the conversion price from \$0.03 to \$0.02 per share on the Series C and from \$0.10 to \$0.02 per share on the Series D on the total 147 shares and 930 shares, respectively, of Series C Preferred Stock and Series D Preferred Stock issued and outstanding at August 30, 2013, and which resulted in an increase in the number of common shares issuable, we recognized additional preferred deemed dividends of \$36,000 on the Series C Preferred Stock and \$465,000 on the Series D Preferred Stock. The net loss attributable to common shareholders reflects both the net loss and the deemed dividend. As a result of the \$500,000 loan and security agreement entered into on September 30, 2013, we issued to the lender 50 shares of our Series D Preferred stock for the \$50,000 loan origination fee.

During the year ended December 31, 2014, the remaining 467 shares of Series B Preferred Stock were converted into 21,020,015 shares of common stock, the remaining 87 shares of Series C Preferred Stock were converted into 4,333,350 shares of common stock and the remaining 860 shares of Series D Preferred Stock were converted into 43,000,000 shares of common stock.

Cash Flow Analysis

Our primary capital requirement is to fund purchases of solar panels and inverters. Significant sources of liquidity are cash on hand, cash flows from operating activities, working capital and proceeds from equity financings. As of March 31, 2015, we had approximately \$135,000 in cash on hand. As of December 31, 2014, we had approximately \$62,000 in cash on hand.

Cash used in operating activities was approximately \$628,000 for the three months ended March 31, 2015. Cash used in operating activities was primarily due to our net loss adjusted for non-cash items of \$99,000, a \$67,000 decrease in accounts receivable and an \$84,000 increase in accrued liabilities and accrued warranty, partially offset by a \$124,000 decrease in accounts payable. The increases and decreases in assets and liabilities were primarily due to the timing of payments and receipts. Cash used in operating activities was approximately \$1.2 million for the year ended December 31, 2014. Net cash used by operating activities was primarily due our net loss adjusted for non-cash items of \$2.0 million, partially offset by a \$412,000 decrease in accounts receivable, a \$159,000 decrease in prepaid expenses and other current assets, a \$58,000 decrease in inventory, and a \$325,000 increase in accounts payable. The increases and decreases in assets and liabilities were primarily due to the timing of payments and receipts.

Cash used in investing activities was approximately \$42,000 for the three months ended March 31, 2015. Cash used in investing activities was due to the acquisition of patents.

Cash provided by financing activities was approximately \$744,000 for the three months ended March 31, 2015. During the three months ended March 31, 2015, we received \$780,000 in proceeds from securities purchase agreement, partially offset by \$36,000 from the repayment of notes payable. Cash provided by financing activities was approximately \$1.1 million for the year ended December 31, 2014. During the year ended December 31, 2014, we received \$600,000 in proceeds from borrowings on long-term debt and \$677,000 in proceeds from an Equity Purchase Agreement, less \$37,000 in payment of placement agent fees, and repayment of \$142,000 in notes payable.

Application of Critical Accounting Policies and Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires estimates and assumptions that affect the reporting of assets, liabilities, sales and expenses, and the disclosure of contingent assets and liabilities. Note 2 to our consolidated financial statements for the year ended December 31, 2014, provides a summary of our significant accounting policies, which are all in accordance with generally accepted accounting policies in the United States. Certain of our accounting policies are critical to understanding our consolidated financial statements, because their application requires management to make assumptions about future results and depends to a large extent on management's judgment, because past results have fluctuated and are expected to continue to do so in the future.

We believe that the application of the accounting policies described in the following paragraphs is highly dependent on critical estimates and assumptions that are inherently uncertain and highly susceptible to change. For all these policies, we caution that future events rarely develop exactly as estimated, and the best estimates routinely require adjustment. On an ongoing basis, we evaluate our estimates and assumptions, including those discussed below.

Revenue recognition. Revenue from sales of products is recognized when: (1) persuasive evidence of an arrangement exists, (2) delivery has occurred or services have been rendered, (3) the sale price is fixed or determinable, and (4) collection of the related receivable is reasonably assured. We recognize revenue when the solar power systems are shipped to the customer. Revenue from installation of a system is recognized when (1) persuasive evidence of an arrangement exists, (2) delivery has occurred or services have been rendered, (3) the sales price is fixed or determinable, and (4) collection of the related receivable is reasonably assured. In general, we recognize revenue upon

completion of a system installation for residential installations and we recognize revenue under the percentage-of-completion method for commercial installations. Revenue recognition methods for revenue streams that fall under other categories are determined based on facts and circumstances.

Discontinued operations. Discontinued operations are presented and accounted for in accordance with Accounting Standards Codification (ASC) 360, "Impairment or Disposal of Long-Lived Assets," (ASC 360). When a qualifying component of the Company is disposed of or has been classified as held for sale, the operating results of that component are removed from continuing operations for all periods presented and displayed as discontinued operations if: (a) elimination of the component's operations and cash flows from the Company's ongoing operations has occurred (or will occur) and (b) significant continuing involvement by the Company in the component's operations does not exist after the disposal transaction. On September 10, 2010, we announced that we were exiting the solar panel installation business. The exit from the installation business was essentially completed at the end of the fourth quarter of 2010. The exit from the installation business was therefore classified as discontinued operations for all periods presented under the requirements of ASC 360. In the fourth quarter of 2014, we re-entered the residential and commercial installation business in the. As a result of re-entering the installation business, we reclassified our discontinued operations into continuing operations.

Inventory. Inventory is stated at the lower of cost (on an average basis) or market value. We determine cost based on our weighted-average purchase price and include both the costs of acquisition and the shipping costs in our inventory. We regularly review the cost of inventory against its estimated market value and record a lower of cost or market write-down to cost of goods sold, if any inventory has a cost in excess of estimated market value. Our inventory generally has a long life cycle and obsolescence has not historically been a significant factor in its valuation.

Long-lived assets. We periodically review our property and equipment and identifiable intangible assets for possible impairment whenever facts and circumstances indicate that the carrying amount may not be fully recoverable. Assumptions and estimates used in the evaluation of impairment may affect the carrying value of long-lived assets, which could result in impairment charges in future periods. Significant assumptions and estimates include the projected cash flows based upon estimated revenue and expense growth rates and the discount rate applied to expected cash flows. In addition, our depreciation and amortization policies reflect judgments on the estimated useful lives of assets.

Patent costs. We capitalize external legal costs and filing fees associated with obtaining or defending our patents and amortize these costs using the straight-line method over the shorter of the legal life of the patent or its economic life. We believe the remaining useful lives we assigned to these assets, approximately 10 years as of December 31, 2014, are reasonable. We periodically review our patents to determine whether any such costs have been impaired and are no longer being used. To the extent we no longer use certain patents, the associated costs will be written-off at that time.

Stock-based compensation. We use the Black-Scholes-Merton Option Pricing Model (Black-Scholes) to estimate fair value of our employee and our non-employee director stock-based awards. Black-Scholes requires various judgmental assumptions, including estimating stock price volatility, expected option life and forfeiture rates. We measure compensation expense for non-employee stock-based compensation under ASC 505-50, "Equity-Based Payments to Non-Employees." The fair value of the option issued is used to measure the transaction, as this is more reliable than the fair value of the services received. The estimated fair value is measured utilizing Black-Scholes using the value of our common stock on the date that the commitment for performance by the counterparty has been reached or the counterparty's performance is complete.

Warranty provision. The manufacturer directly warrants the solar panels and inverters for a range from 15 to 25 years. We warrant the balance of system components of our products against defects in material and workmanship for five years. We assist our customers in the event of a claim under the manufacturer warranty to replace a defective solar panel or inverter.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements (as defined in the applicable regulations) that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

Inflation

We believe that inflation has not had a material impact on our historical results of operations; however, there can be no assurance that our business will not be affected by inflation in the future.

Seasonality

Our quarterly operating results may vary significantly from quarter to quarter as a result of seasonal changes in weather as well as state or Federal subsidies. Historically, sales are highest during the third and fourth quarters as a result of good weather and robust bookings in the second quarter.

Significant Accounting Policies and Estimates

There have been no material changes or developments to the significant accounting policies discussed in our Notes to Financial Statements for the quarter ended March 31, 2015 or accounting pronouncements issued or adopted, except as described below.

DIRECTORS, EXECUTIVE OFFICERS, PROMOTERS AND CONTROL PERSONS

Executive Officers

The following table contains information with respect to our current executive officers and directors.

Name	Age	Position
Steven Chan	47	President, Chief Executive Officer, Interim Chief Financial Officer, Treasurer, Secretary and Director
Wei-Tai Kwok	51	Chief Operating Officer
Mark L. Kalow	60	Chairman of the Board of Directors
Ron Kenedi	67	Director

Each director holds office until the next annual meeting of stockholders or until their successor has been duly elected and qualified. Executive officers are elected annually and serve at the discretion of our board of directors.

Steven Chan, Chief Executive Officer, President of the Company, Interim Chief Financial Officer and Director . Mr. Chan has been our Chief Executive Officer, President, acting Chief Financial Officer and a Director since April 2014. Our Nominating and Corporate Governance Committee decided that Mr. Chan should serve on our Board based on his expertise in the solar industry and his prior management roles with other solar companies. Mr. Chan previously served as the Vice President of NRG Energy (NYSE: NRG) from May 2012 to November 2013 serving as head of residential solar for its NRG Home Solar business. Prior to that, Mr. Chan served as EVP, Strategy and System Sales at GCL-Poly Energy Holdings Limited (Hong Kong: 3800) from September 2011 to May 2012 where he helped to build out a system sales division for GCL in North America including establishing and serving as a board member at Sunora Energy Solutions, a joint venture with NRG Energy to focus on utility and commercial solar installations. From 2006 until 2011 he held various positions at Suntech Power Holdings Co., Ltd. (OTC: STPFQ), which included serving as the President of Suntech America and as Suntech's President of Global Sales and Marketing, Chief Strategy Officer and VP Business Development.

Wei-Tai Kwok, Chief Operating Officer. Mr. Kwok joined the Company as our Chief Operating Officer in November 2014 and was appointed as a Director in March 2015. Our Nominating and Corporate Governance Committee decided that Mr. Kwok should serve on our Board based on his expertise in the solar industry and his prior management roles with other solar companies. Prior to this, Mr. Kwok was Vice President of Operations in the NRG Home Solar division of NRG Energy, with responsibility for supply chain, procurement, logistics, engineering and O&M. From 2009-2012, Mr. Kwok was Vice President of Marketing at Suntech Power, where he had responsibility for growing the brand globally across the Americas, Europe/Middle East and Africa, Asia Pacific, China and Japan. Prior to Suntech, Mr. Kwok spent 17 years in general management as a marketing executive. He was a Managing Director for Isobar, the wholly-owned digital agency network of Aegis Group plc, one of the world's largest marketing communications conglomerates now owned by Dentsu. He was previously President & CEO of Dae Advertising, a top Asian American advertising agency based in San Francisco which he helped co-found in 1990. Mr. Kwok is a graduate of Yale University with a B.A. in Economics & Political Science.

Mark Kalow, Director. Mr. Kalow has been a director since December 2011 and was appointed as Chairman of the Board of Directors in November 2013. Mr. Kalow's financial management background provides him with a broad understanding of the financial issues facing the Company, the financial markets and the financing opportunities available to the Company. His prior service on the board of other public companies has provided him with a strong corporate governance expertise and an understanding of the proper role and function of the Board. Since 2004, Mr.

Kalow has been a Managing Director at Soquel Group, a consulting firm specializing in Intellectual Property and Business Development. He currently serves on the board of directors of Rope Partner (2010), a wind energy service company, Geary LSF (2002), an e-marketing services company, Propell Corporation (PROP.OB) (2008), a supplier of e-commerce solutions, Dogfish Software (2008), a software services provider, and Pure Depth, Inc. (2006), a display technology licensing company. From 2004 through 2008, Mr. Kalow served on the Board of Photoworks, Inc., and from 1998 through 1999, served as CEO of Live Picture, Inc. Mr. Kalow graduated in 1975 with a Bachelor of Science degree in Management from the Massachusetts Institute of Technology and in 1977 received a Masters in Business Administration with a concentration in financial management from the University of Chicago.

Ron Kenedi, Director. Mr. Kenedi has been a director since January 2011. The Board's Nominating and Corporate Governance Committee decided that Mr. Kenedi should serve on the Company's Board based on his personal and professional qualities, including his proven integrity, absence of conflicts of interest, sound judgment, achievements in business and company management, business understanding, and available time to dedicate to the role. Mr. Kenedi's management roles with other solar energy companies and his expertise in the solar industry make him a valuable member of our Board. From 2012 to the present, Mr. Kenedi has been the President of Ron Kenedi Consulting. Mr. Kenedi was the President of LDK Solar USA from 2011 to 2012. From 2002 through 2010, Mr. Kenedi served as vice president of Sharp Electronics Corporation's Solar Energy Solutions Group. Mr. Kenedi was responsible for the establishment and expansion of Sharp's North American solar division and played a key role in achieving several milestones in the solar arena. From 1999 to 2002, Mr. Kenedi was vice president of sales and marketing for Photocomm/Kyocera Solar. In this capacity, he created and developed the organization's dealer network, and expanded Kyocera's U.S. market share from 5 to 20 percent within two years. Mr. Kenedi launched "SOLA in NOLA," which supplied solar power systems to New Orleans communities impacted by Hurricane Katrina. Mr. Kenedi has served as a solar industry spokesperson and is a member of the Solar Energy Industry Association (SEIA), the California Solar Energy Industry Association (CALSEIA), the Arizona Solar Energy Industry Association (ARISEIA) and The International Solar Energy Society (ISEIA). In 1969, Mr. Kenedi earned a Bachelor of Arts (Magnum cum Laude), from the State University of New York at Stony Brook.

Summary Compensation Table

The following Summary Compensation Table sets forth certain information about the compensation paid, earned or accrued for services rendered to us in all capacities for the years ended December 31, 2014 and 2013 by our President, Chief Executive Officer, Chief Financial Officer and Chief Operating Officer and our other most highly compensated executive officers (our "Named Executive Officers"). We did not have any other executive officers in the year ended December 31, 2014 and 2013 that were paid or earned compensation in excess of \$100,000 for services rendered during such years.

Name and Principal Position	Year	Salary	Stock Awards(1)	Option Awards(1)	All Other Compensation	Total
Steven Chan, President, Chief Executive Officer, interim Chief Financial Officer and Treasurer	2014	\$ 173,296	\$ —	\$ —	597(3)	\$ 173,893
Wei-Tai Kwok, Chief Operating Officer	2014	\$ 24,433	\$ —	\$ —	—	\$ 24,433
Margaret Randazzo, former President, Chief Executive Officer, Chief Financial Officer, Secretary and Treasurer	2014	\$ 123,700	\$ 21,339	\$ —	350(2)	\$ 145,389
	2013	\$ 216,563	\$ 9,430	\$ —	1,200(2)	\$ 227,193

(1) The amounts in this column represent the aggregate grant date fair values of the restricted stock and the option awards granted to the executives in each of the years in accordance with stock compensation accounting. See "Stock Incentive Plan" footnote in the Notes to our Consolidated Financial Statements for the

year ended December 31, 2013, for a discussion of all assumptions made by us in determining the valuation of the equity awards.

(2) Represents reimbursement for cell phone expense.

(3) Represents reimbursement of medical insurance.

Outstanding Equity Awards at Year-End

The following table sets forth certain information relating to equity awards outstanding as of December 31, 2014 for the Named Executive Officers.

Name	Grant Date	Option Awards				Stock Awards	
		Number of Securities Underlying Unexercised Options Exercisable (#)	Number of Securities Underlying Unexercised Options Unexercisable (#)	Option Exercise Price (\$/Sh)	Option Expiration Date	Number of Shares of Stock that Have Not Vested (#)	Market Value of Shares or Units that Have Not Vested (\$)
Steven Chan							
	04/14/2014	1,125,000(1)	7,875,000(1)	\$ 0.02	04/13/2019	—	—
	08/06/2014	250,000(2)	2,750,020(2)	\$ 0.02	08/05/2019	—	—
	08/06/2014	—(3)	3,000,000(3)	\$ 0.02	08/05/2019	—	—
Wei-Tai Kwok							
	11/07/2014	—(4)	6,000,000(4)	\$ 0.02	11/06/2019	—	—
	11/07/2014	—(2)	3,000,000(2)	0.02	11/06/2019	—	—
Margaret Randazzo							
	12/04/2009	18,750(5)	—(5)	\$ 4.00	12/03/2014	—	—
	07/26/2010	18,750(5)	—(5)	\$ 0.87	07/26/2015	—	—
	02/15/2011	62,500(5)	—(5)	\$ 2.16	02/14/2016	—	—
	11/06/2013	1,666,500(5)	833,500(5)	\$ 0.03	11/05/2018	—	—

(1) Options vest as to 1/16th of the shares subject to the option on the six month anniversary of the date of issuance, another 1/16th vesting two months after such six months and thereafter vesting as to 1/16th each subsequent quarter.

(2) Options vest as to 1/12th of the shares subject to the option on a quarterly basis over a 3 year vesting period.

(3) Options vest as to 100% of the shares subject to the option on the five year anniversary from the date of grant, subject to accelerated vesting based on certain performance-based metrics.

(4) Options fully vest on the fifth anniversary of the date of grant; however the options may be accelerated in increments of 600,000 options depending upon achievement of specified performance milestones.

(5) Options granted vest over a three-year period beginning on each anniversary of the date of grant.

Option Exercises and Stock Vested

The following table sets forth certain information relating to the exercise of stock options and the vesting of stock awards during the year ended December 31, 2014 for each Named Executive Officers.

Name	Option Awards		Stock Awards	
	Number of Shares Acquired on Exercise (#)	Value Realized on Exercise (\$)	Number of Shares Acquired on Vesting (#)	Value Realized on Vesting (\$)
Steven Chan	—	\$ —	—	\$ —
Wei-Tai Kwok	—	\$ —	—	\$ —
Margaret Randazzo	—	\$ —	938,750	\$ 21,339

Employment Agreements and Post Termination Compensation

On May 7, 2012, Margaret Randazzo was appointed as the Company's interim chief executive officer, president, and secretary. She also continued in her capacity as the chief financial officer. In connection with her appointment as the Company's interim CEO, the Company entered into an employment agreement pursuant to which the Company agreed to pay Ms. Randazzo an annual gross salary of \$225,000 until December 31, 2012 or the earlier closing of the proposed merger transaction which we had been negotiating, upon which a reasonably acceptable successor position would be agreed upon between the parties, with a salary of not less than \$225,000 on an annual basis, and a target bonus not less than 45% of the base salary. In addition to Ms. Randazzo's salary as interim CEO, she was also eligible to participate in the Company's bonus program (with a target bonus of \$100,000, of which 50% would be payable in stock of the Company or a successor employer (valued at the VWAP (Volume Weighted Average Price) for the 10 trading days preceding the consummation of the merger) and 50% would be payable in cash in the last payroll distribution of December 2012), plus health and other benefits programs. There was no bonus paid to Ms. Randazzo's for the year ended December 31, 2013, due to the Company's limited financial resources. On July 18, 2013 the Company terminated its merger agreement with CBD. Ms. Randazzo resigned her employment with us in July 2014.

In connection with his appointment, Mr. Chan entered into an employment agreement with the Company date April 14, 2014. Pursuant to the Employment Agreement, Mr. Chan is entitled to an annual base salary of \$250,000 and is eligible for discretionary performance bonus payments. For the years ended December 31, 2014 and December 31, 2015, the annual bonus that Executive is eligible to receive is a bonus of options exercisable for an additional one million (1,000,000) and one million five hundred thousand (1,500,000) shares of common stock, respectively, in each case subject to approval of the both the Compensation Committee and the Board of Directors. Additionally, Mr. Chan was granted options to purchase 9,000,000 shares of the Company's common stock with an exercise price equal to the Company's per share market price on the date of issue. These options will vest as to 1/16th of the shares subject to the option on the six month anniversary of the date of issuance, another 1/16th vesting two months after such six months and thereafter vesting as to 1/16th each subsequent quarter. Mr. Chan also executed a related agreement that includes confidentiality obligations and inventions assignments by Mr. Chan.

On April 14, 2015, Mr. Chan and the Company amended his employment agreement to provide for a “Sale of the Company Bonus.” Pursuant to the amended agreement, Mr. Chan will be entitled to 5.5% of any sale proceeds should the Company or substantially all of its assets be sold. Additionally, the amended agreement provides that in the case of Mr. Chan’s termination other than for cause or in the event of a change of control, then Mr. Chan will be entitled to six months’ salary, six months’ COBRA payments, and 100% vesting his outstanding but unvested stock options.

In connection with his appointment, Mr. Kwok entered into an employment agreement with the Company dated November 7, 2014. Pursuant to the Employment Agreement, Mr. Kwok will be entitled to an annual base salary of \$165,000 and will be eligible for discretionary performance bonus payments. For the year ended December 31, 2015, the annual bonus that Mr. Kwok is eligible to receive is a bonus of up to \$45,000. Additionally, Mr. Kwok was granted options to purchase 9 million shares of the Company’s common stock with an exercise price equal to the Company’s per share market price on the date of issue. Of the 9 million options, 3 million of these options will vest as to one twelfth (1/12th) of the shares each quarter, so that the option will be fully vested and exercisable three years from the start date, subject to Mr. Kwok continuing to provide services to the Company through the relevant vesting dates, and 6 million of these options shall vest upon the fifth anniversary of the start date; provided, that options may be accelerated in increments of 600,000 depending upon achievement by Mr. Kwok of specified performance milestones as set forth in a separate option agreement which shall be measured as of the end of each calendar quarter. Mr. Kwok also executed a related agreement that includes confidentiality obligations and inventions assignments by Mr. Kwok.

On April 14, 2015, Mr. Kwok and the Company amended his employment agreement to provide for a “Sale of the Company Bonus.” Pursuant to the amended agreement, Mr. Kwok will be entitled to 4.5% of any sale proceeds should the Company or substantially all of its assets be sold. Additionally, the amended agreement provides that in the case of Mr. Kwok’s termination other than for cause or in the event of a change of control, then Mr. Kwok will be entitled to six months’ salary, six months’ COBRA payments, and 100% vesting his outstanding but unvested stock options.

Director Compensation

The following table sets forth certain information concerning the compensation paid or earned by the Directors who were not Named Executive Officers for services rendered in all capacities during the fiscal year ended December 31, 2014.

Name	Fees Earned or Paid in Cash	Restricted Stock Awards Aggregate Fair Value	Stock Option Awards Aggregate Fair Value	Total
Mark L. Kalow	\$ 12,000	\$ —	\$ —	12,000
Ron Kenedi	\$ —	\$ —	\$ —	—

Committees of the Board of Directors and Meeting Attendance

The Company has standing Nominating and Corporate Governance, Audit, and Compensation Committees of the Board of Directors.

The Nominating and Corporate Governance Committee. The Nominating and Corporate Governance Committee (the “Nominating Committee”) is comprised of Messrs. Kalow and Kenedi . The Nominating Committee of the Board of Directors performs the functions typical of a nominating committee, including: (i) developing and recommending corporate governance principles and procedures applicable to the Board of Directors and the Company’s employees; (ii) recommending committee composition and assignments; (iii) identifying individuals qualified to become directors; (iv) recommending director nominees; (v) recommending whether incumbent directors should be nominated for re-election to the Board of Directors and (vi) reviewing the adequacy of the Nominating Committee charter.

The Audit Committee. The Audit Committee is comprised of Mr. Kalow. The Audit Committee of the Board of Directors has the authority and responsibility to select, evaluate and, when appropriate, replace the company’s independent registered public accounting firm. The Audit Committee monitors the activities of the Company’s external auditors, including the audit scope, the external audit fees, auditor independence matters and the extent to which the independent auditors may be retained to perform advisory services. The Audit Committee also reviews the results of the external audit work to assess the adequacy and appropriateness of the Company’s financial and accounting controls. The Audit Committee reviews changes in accounting standards that impact the Company’s financial statements and discusses with management major events, including legal matters and tax audits, which may have significant financial impact or are the subject of discussions with the independent auditors. In addition, the Audit Committee oversees the Company’s internal audit and compliance programs.

The Compensation Committee. The Compensation Committee is comprised of Mr. Kalow. The Compensation Committee administers the Company’s Stock Plan, including the review and grant of stock options and restricted stock to officers, directors and other employees under the Stock Plan. The Compensation Committee also reviews and approves various other Company compensation policies and matters, and reviews and approves salaries and other matters relating to compensation of the executive officers of the Company. The Compensation Committee reviews and approves on an annual basis the corporate goals and objectives with respect to the compensation for the Company’s Chief Executive Officer and other executive officers. The Committee evaluates at least once a year the Chief Executive Officer and other executive officers’ performance in light of these established goals and objectives and based upon these evaluations shall recommend to the full Board the Chief Executive Officer and other executive officers’ annual compensation, including salary, bonus, incentive and equity compensation. The Compensation Committee develops and periodically assesses the Compensation Committee’s compensation policies applicable to the Company’s executive officers and directors, including the relationship of corporate performance to executive compensation. The Compensation Committee reviews and recommends to the Board appropriate director compensation programs for service as directors, committee chairs and committee members.

SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The following table sets forth certain information, as of July 17, 2015, with respect to the beneficial ownership of our common stock by: (i) each holder of more than five percent (5%) of the outstanding shares of our common stock; (ii) our executive officers and directors; and (iii) all our executive officers and directors as a group. The Company's issued and outstanding voting securities at the close of business on July 17, 2015, consisted of 400,040,909, shares of common stock.

Unless otherwise indicated below, to our knowledge, all persons listed below have sole voting and investment power with respect to their shares of common stock, except to the extent authority is shared by spouses under applicable law. Unless otherwise indicated below, each entity or person listed below maintains an address of c/o 48900 Milmont Dr., Fremont, California 94538

The number of shares beneficially owned by each stockholder is determined under rules promulgated by the Securities and Exchange Commission. The information is not necessarily indicative of beneficial ownership for any other purpose. Under these rules, beneficial ownership includes any shares as to which the individual or entity has sole or shared voting or investment power and any shares as to which the individual or entity has the right to acquire beneficial ownership within 60 days after July 17, 2015 through the exercise of any stock option, warrant or other right. The inclusion in the following table of those shares, however, does not constitute an admission that the named stockholder is a direct or indirect beneficial owner.

Name and Address of Beneficial Owner (1)		Amount and Nature of Beneficial Ownership	Percent of Class (2)
Alpha Capital Anstalt Pradafant 7, Furstentums 9490 Vaduz, Liechtenstein	(3)	44,448,987	9.99%
Mark Kalow	(4)	786,586	*
Ron Kenedi	(5)	807,076	*
Steven Chan	(6)	3,562,500	*
Wei-Tai Kwok	(7)	750,000	*
All Executive officers and directors as a group (4 persons, including the executive officer and directors names above)			1.5%

* Less than 1%

(1) Unless otherwise indicated, the address for each of the stockholders is c/o Andalay Solar, Inc. 48900 Milmont Dr., Fremont, California 94531.

(2) The applicable percentage of ownership for each beneficial owner is based on 400,040,909 shares of common stock outstanding as of July 17, 2015. In calculating the number of shares beneficially owned by a stockholder and the percentage of ownership of that stockholder, shares of common stock issuable upon the exercise of options or warrants, or the conversion of other securities held by that stockholder, that are exercisable within 60 days, are deemed outstanding for that holder; however, such shares are not deemed outstanding for computing the percentage ownership of any other stockholder.

(3) Includes 44,448,987 shares of common stock, in aggregate, that may be obtained upon conversion of outstanding convertible notes payable. The holder currently holds \$500,000 in convertible notes, which are convertible into 50,000,000 shares. In addition, the holder currently holds warrants to purchase 21,428,437 shares of common stock.

- (4) Includes 663,370 shares of nonqualified stock options which are exercisable for shares of Andalay Solar's common stock within 60 days of July 17, 2015. Does not include 325,000 shares of nonqualified stock issuable upon the exercise of options which vest in November 2015.
- (5) Includes 674,238 shares of nonqualified stock options which are exercisable for shares of Andalay Solar's common stock within 60 days of July 17, 2015. Does not include 325,000 shares of nonqualified stock issuable upon the exercise of options which vest in November 2015.
- (6) Includes 3,562,500 shares of nonqualified stock options which are exercisable for shares of Andalay Solar's common stock within 60 days of July 17, 2015. Does not include 11,437,500 shares of nonqualified stock issuable upon the exercise of options which vest in various dates over the next four and a half years.
- (7) Includes 750,000 shares of nonqualified stock options which are exercisable for shares of Andalay Solar's common stock within 60 days of July 17, 2015. Does not include 8,250,000 shares of nonqualified stock issuable upon the exercise of options which vest over the next five years.

TRADING MARKET

Our common stock became eligible for trading on the OTCQB on September 6, 2012. On May 15, 2015, we began trading on the OTCPink and then on July 20, 2015, our stock became eligible for trading on the OTCQB. Our common stock is quoted on the OTCQB under the symbol "WEST". The closing price of our stock on July 17, 2015, was \$0.01. There is currently a limited trading market for our common stock on the OTCQB. The shares will be sold at the prevailing market price at the time of sale or privately negotiated prices.

SELLING SECURITY HOLDER

The shares to be offered by the selling security holder were issued in private placement transactions by us, each of which was exempt from the registration requirements of the Securities Act. The shares offered hereby are "restricted" securities under applicable federal and state securities laws and are being registered under the Securities Act, to give the selling security holder the opportunity to publicly sell these shares. This prospectus is part of a registration statement on Form S-1 filed by us with the Securities and Exchange Commission under the Securities Act covering the resale of such shares of our common stock from time to time by the selling security holder. No estimate can be given as to the amount or percentage of our common stock that will be held by the selling security holder after any sales made pursuant to this prospectus because the selling security holder is not required to sell any of the shares being registered under this prospectus. The following table assumes that the selling security holder will sell all of the shares listed in this prospectus.

The following table sets forth the name of each person who is offering for resale shares of common stock covered by this prospectus, the beneficial ownership of each selling security holder, the number of shares of common stock that may be sold in this offering and the number of shares of common stock each will own after the offering, assuming they sell all of the shares offered. The term "selling security holder" includes the stockholder listed below and its transferees, assignees, pledges, donees or other successors. Beneficial ownership is determined in accordance with the rules of the Securities and Exchange Commission and generally includes voting or investment power with respect to securities. There are no shares of common stock subject to options, warrants and convertible securities.

Shareholder and Name of Person Controlling	Amount of Shares owned before Offering	Number of shares offered	Amount of shares owned after Offering	Percent of shares held after Offering
Southridge Partners II LP (1)	-	150,000,000	-	*%
Total	-	150,000,000	-	*%

- Less than 1%.

(1) Steve Hicks is the managing member of Southridge Advisors II, LLC, the general partner of Southridge and has voting and investment control over Southridge.

RELATIONSHIP BETWEEN THE ISSUER AND THE SELLING SECURITY HOLDER

Other than as set forth below, the selling security holder has not at any time during the past three years acted as one of our employees, officers or directors or had a material relationship with us. On February 20, 2013, we entered into a consulting agreement with SC Advisors Inc., an affiliate of the selling security holder, to provide variety of financial management, business consulting and advisory services. These services included cash flow projection, financial statement preparation, balance sheet optimization and debt restructuring advice, as well as third party service provider support, such as-coordinating functions with auditors and legal counsel, and interfacing with investor/public relations to increase our awareness in the financial marketplace and help keep our shareholders abreast of our current developments. In consideration of its services under the consulting agreement, since March 1, 2013, SC Advisors Inc. received a monthly fee of thirty thousand dollars (\$30,000), in the form of shares of our Series D Preferred, valued at the \$1,000 stated value per share of the Series D Preferred or convertible notes. On November 1 and December 1, 2013, and on January 1, February 1 and March 1, 2014, we issued convertible notes to our financial advisory firm in the principal amount of \$30,000 each for a total of \$150,000, which matured on October 31 and November 30 and December 31, 2014, and on January 31 and February 28, 2015, respectively. On April 1, May 1 and June 1, 2014, we issued convertible notes to our financial advisory firm in the principal amount of \$20,000 each, for a total of \$60,000, which matured on March 31, April 30 and May 31, 2015, respectively. The Series D Preferred and all of the convertible notes have been converted in shares of our common stock and there is no preferred stock or convertible notes outstanding. The consulting agreement may be terminated by either party without cause upon thirty (30) days prior written notice; provided however that if we had terminated the consulting agreement without cause during the 4 month period following its effective date, we would have still remained obligated to pay the consulting fee through the end of such term. The consulting agreement may also be terminated by either party for cause at any time. We have further agreed to indemnify SC Advisors Inc. against any actions, losses, damages, claims, liabilities, costs and expenses (including without limitation, reasonable legal fees and expenses) in any way arising out of or relating to the consulting agreement, unless it is due to gross negligence on their part. In addition, on January 22, 2014, we entered into a debt settlement arrangement with ASC Recap, LLC, an affiliate of the selling shareholder, pursuant to which we agreed to issue shares of our common stock in a 3(a)(10) proceeding to ASC Recap, LLC as payment for certain prior debt of ours that ASC Recap LLC, acquired from our prior creditors at a discount. We agreed to pay ASC Recap, LLC through the issuance of shares of our common stock an amount equal to 250% of the discounted amount ASC Recap, LLC paid for the debit, which is substantially below the original amount we owed to the prior creditors. Upon payment from ASC Recap, LLC the creditors provided us with a full release from all liability owed to them. On February 21, 2014, ASC Recap filed with the Circuit Court of the Second Judicial Circuit, Leon County, Florida (the "Court") an amended complaint and demand for payment of the debt it acquired from one of our creditors. On February 26, 2014, we entered into a Settlement Agreement and Stipulation with ASC Recap LLC that was filed with the Court pursuant to which we agreed, subject to court approval, to issue shares of our common stock in a Section 3(a) (10) proceeding that generate proceeds in the amount of \$250,000 in full settlement of a claim in the amount of \$1,027,705 that ASC Recap acquired from one Creditor (the value of the stock that we agreed to issue was two hundred and fifty percent (250%) of the discounted purchase price ASC paid to purchase the debt from the Creditor, and approximately 25% of the original amount we owed to the Creditor). All amounts were paid in April 2014.

We entered into the Prior Equity Purchase Agreement with Southridge in January 2014 pursuant to which we issued 35,000,000 shares of our common stock and we received \$677,000 from the sale of the common stock. We paid Southridge a commitment fee of 1,000,000 shares of our common stock. On December 9, 2014, we terminated the Prior Equity Purchase Agreement with Southridge that was entered into in January 2014 and entered into the December Equity Purchase Agreement. To date, we have issued to Southridge 84,113,042 shares of common stock from the December Equity Agreement.

PLAN OF DISTRIBUTION

The selling security holder of our common stock and any of its transferees, pledgees, assignees, donees, and successors-in-interest may, from time to time, sell any or all of their shares of common stock on the stock exchange, market or trading facility on which the shares are traded or in private transactions. These sales may be at fixed or negotiated prices. The selling security holder may use any one or more of the following methods when selling shares:

- ordinary brokerage transactions and transactions in which the broker-dealer solicits purchasers;
- block trades in which the broker-dealer will attempt to sell the shares as agent but may position and resell a portion of the block as principal to facilitate the transaction;
- purchases by a broker-dealer as principal and resale by the broker-dealer for its account;
- an exchange distribution in accordance with the rules of the applicable exchange;
- privately negotiated transactions;
- broker-dealers may agree with the selling security holders to sell a specified number of such shares at a stipulated price per share;
- a combination of any such methods of sale; or
- any other method permitted pursuant to applicable law.

Broker-dealers engaged by the selling security holder may arrange for other broker-dealers to participate in sales. Broker-dealers may receive commissions or discounts from the selling security holder (or, if any broker-dealer acts as agent for the purchaser of shares, from the purchaser) in amounts to be negotiated. The selling security holder does not expect these commissions and discounts relating to its sales of shares to exceed what is customary in the types of transactions involved.

The selling security holder and any broker-dealers or agents that are involved in selling the shares of common stock are “underwriters” within the meaning of the Securities Act in connection with such sales. In such event, any commissions received by such broker-dealers or agents and any profit on the resale of the shares purchased by them is deemed to be underwriting commissions or discounts under the Securities Act. Because the selling security holder is an underwriter within the meaning of the Securities Act, it will be subject to the prospectus delivery requirements of the Securities Act. Discounts, concessions, commissions and similar selling expenses, if any, that can be attributed to the sale of common stock will be paid by the selling security holder and/or the purchasers. The selling security holder has represented and warranted to our company that it acquired the securities subject to this registration statement in the ordinary course of such selling security holder’s business and, at the time of its purchase of such securities such selling security holder had no agreements or understandings, directly or indirectly, with any person to distribute any such securities.

There is no underwriter or coordinating broker acting in connection with the proposed sale of the resale shares by the selling security holder. We are required to pay certain fees and expenses incurred by us incident to the registration of the shares. We have agreed to indemnify the selling security holder against certain losses, claims, damages and liabilities, including liabilities under the Securities Act.

The selling security holder may from time to time pledge or grant a security interest in some or all of the shares owned by it, and, if it defaults in the performance of its secured obligations, the pledgees or secured parties may offer and sell shares of common stock from time to time under this prospectus, or under an amendment to this prospectus under Rule 424(b)(3) or other applicable provision of the Securities Act amending the list of selling security holders to include the pledgee, transferee or other successors-in-interest as selling security holders under this prospectus. Upon our company being notified in writing by the selling security holder that any material arrangement has been entered into with a broker-dealer for the sale of common stock through a block trade, special offering, exchange distribution or secondary distribution or a purchase by a broker or dealer, a supplement to this prospectus will be filed, if required, pursuant to Rule 424(b) under the Securities Act, disclosing: (i) the name of each such selling security holder and of the participating broker-dealer(s); (ii) the number of shares involved; (iii) the price at which such the shares of common stock were sold; (iv) the commissions paid or discounts or concessions allowed to such broker-dealer(s), where applicable; (v) that such broker-dealer(s) did not conduct any investigation to verify the information set out or incorporated by reference in this prospectus; and (vi) other facts material to the transaction.

Under applicable rules and regulations under the Exchange Act, any person engaged in the distribution of the resale shares may not simultaneously engage in market making activities with respect to our common stock for a period of two business days prior to the commencement of the distribution. In addition, the selling security holders will be subject to applicable provisions of the Exchange Act and the rules and regulations thereunder, including Regulation M, which may limit the timing of purchases and sales of shares of our common stock by the selling security holders or any other person. We will make copies of this prospectus available to the selling security holders and have informed them of the need to deliver a copy of this prospectus to each purchaser at or prior to the time of the sale.

Although Southridge has agreed not to enter into any “short sales” of our common stock, sales after delivery of a put notice of a number of shares reasonably expected to be purchased under a put notice shall not be deemed a “short sale.” Accordingly, Southridge may enter into arrangements it deems appropriate with respect to sales of shares of our common stock after it receives a put notice under the December Equity Purchase Agreement so long as such sales or arrangements do not involve more than the number of put shares expected to be purchased by Southridge as specified in the notice.

CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

Our current Board of Directors is comprised of Steven Chan, who is also our CEO, Wei-Tai Kwok, who is also our COO, Mark L. Kalow and Ron Kenedi. Although our common stock is no longer listed on any national securities exchange, for purposes of independence we use the definition of independence applied by The NASDAQ Stock Market LLC. The Board of Directors has determined that, other than Steven Chan and Wei-Tai Kwok, each of the current members of the Board is an “independent director.” On May 8, 2012, Mr. Kalow was appointed “Lead Independent Director.” The Lead Independent Director was established to serve in a lead capacity to coordinate the activities of the other independent directors of the Board of Directors, as required. In the course of the Board of Director’s determination regarding the independence of each non-management director, it considered any transactions, relationships and arrangements as required by the applicable rules and regulations of the SEC. On November 6, 2013, Mr. Kalow was appointed Chairman of the Board of Directors. The Company was not a party to any transaction, relationship or other arrangement with any of its “independent directors” that was considered by our Board of Directors under the Marketplace Rules in the determination of such director’s independence.

Our sole member of the Audit Committee meets the independence requirements prescribed Section 10A of The Securities Exchange Act.

Our policy and procedure for the review, approval or ratification of any related party transaction is to present the proposed transaction approval to the appropriate Committee of our Board of Directors, depending upon the type of transaction – either the Compensation Committee for matters relating to compensation or services, the Audit Committee for general financial transactions, or the Corporate Governance Committee for matters relating to independence or potential conflicts of interest. Each of those Committees is comprised entirely of independent directors. In addition, any request for us to enter into a transaction with an executive officer, director or employee, or any of such persons’ immediate family members or affiliates, must first be presented to our Audit Committee for review, consideration and approval. In approving or rejecting the proposed agreement, our Audit Committee will review each such transaction for potential conflicts of interest or improprieties.

There were no relationships or related party transactions during the years ended December 31, 2014 or 2013 requiring disclosure.

Procedures for Approval of Related Person Transactions

Any request for us to enter into a transaction with an executive officer, director or employee, or any of such persons’ immediate family members or affiliates, must first be presented to our Audit Committee for review, consideration and approval. In approving or rejecting the proposed agreement, our Audit Committee will review each such transaction for potential conflicts of interest or improprieties.

DESCRIPTION OF SECURITIES

We have 1,251,000,000 shares of capital stock authorized under our certificate of incorporation, consisting of 1,250,000,000 shares of common stock and 1,000,000 shares of preferred stock. As of July 17, 2015, we had 400,040,909 shares of common stock outstanding. As of July 17, 2015, we have authorized: (i) 2,000 shares of Series A Convertible Preferred Stock, par value \$0.001, (ii) 4,000 shares of Series B 4% Convertible Preferred Stock, par value \$0.001, (iii) 1,175 shares of our Series C 8% Convertible Preferred Stock, par value \$0.001 and (iv) 1,180 shares of our Series D Convertible Preferred Stock, par value \$0.001, all of which have been converted or cancelled and none of which remain outstanding.

The holders of our common stock are entitled to one vote per share on all matters to be voted on by the shareholders. Subject to preferences that may be applicable to any outstanding shares of Preferred Stock, holders of common stock are entitled to receive ratably such dividends as may be declared by the Board out of funds legally available therefore. If we liquidate, dissolve or wind up, holders of common stock are entitled to share ratably in all assets remaining after payment of liabilities and the liquidation preferences of any outstanding shares of Preferred Stock. Holders of common stock have no preemptive, conversion or subscription rights. There are no redemption or sinking fund provisions applicable to the common stock. All outstanding shares of common stock are, and all shares of common stock to be outstanding upon completion of this offering will be, fully paid and nonassessable. Except as otherwise required by Delaware law, all stockholder action, other than the election of directors, is taken by the vote of a majority of the outstanding shares of common stock voting as a single class present at a meeting of stockholders at which a quorum consisting of a majority of the outstanding shares of common stock is present in person or proxy. The election of directors by our stockholders is determined by a plurality of the votes cast by the stockholders entitled to vote at any meeting held for such purposes at which a quorum consisting of a majority of the outstanding shares of common stock is present in person or proxy.

Warrants

Outstanding Warrants

As of July 17, 2015, we had issued and outstanding a total of 22,148,045 warrants to purchase our common stock outstanding at a weighted-average price of \$0.23.

Registration Rights

We have granted “piggy-back” registration rights to the holders of Series D Preferred to include the underlying shares of common stock issuable upon conversion of the Series D Preferred in future registration statements, if any are filed by us.

On each of August 30, 2013, November 25, 2013, December 19, 2013, January 27, 2014 and February 25, 2014, we entered into a securities purchase agreement with certain institutional accredited investors relating to the sale and issuance of convertible notes each in the principal amount of \$200,000, \$200,000, \$250,000, \$100,000 and \$200,000 that mature August 29, 2015, November 24, 2015, December 19, 2015, January 27, 2016 and February 26, 2016, respectively (the "Convertible Notes"). We have also granted the holder of the \$200,000 Convertible Notes “piggy-back” registration rights to include the underlying shares of common stock issuable upon conversion of the Convertible Notes in future registration statements, if any as are filed by us. The securities purchase agreement that we entered into with the holder of the Convertible Note also provides such holder a right to participate in any of our future debt and equity offerings. The holders of the piggyback registration rights have waived such rights with respect to the registration of securities under the Equity Line. On March 18, 2014, we issued under the Securities Purchase Agreement we entered into with the institutional investor on February 25, 2014 a (i) convertible note in the principal amount of \$300,000 that matures March 18, 2016 and (ii) five-year warrant (with a cashless exercise feature under certain circumstances) to purchase 7,500,000 shares of our common stock at an exercise price of \$0.02 per share, subject to adjustment under certain circumstances. The convertible notes bears interest at the rate of 8% per annum compounded annually, are payable at maturity and the principal and interest outstanding under the convertible notes are convertible into shares of our common stock, at any time after issuance, at the option of the purchaser, at a conversion price equal to \$0.02 per share, subject to adjustment upon the happening of certain events, including stock dividends, stock splits and the issuance of common stock equivalents at a price below the conversion price. Subject to us fulfilling certain conditions, including beneficial ownership limits, the convertible notes are subject to mandatory conversion if the closing price of our common stock for any 20 consecutive days commencing six months after the issue date of the convertible notes equals or exceeds \$0.04 per share. Unless waived in writing by the purchaser, no conversion of the convertible notes can be effected to the extent that as a result of such conversion the purchaser would beneficially own more than 9.99% in the aggregate of our issued and outstanding common stock immediately after giving effect to the issuance of common stock upon conversion.

Preferred Stock

Our Board of Directors has the authority, without action by our stockholders, to designate and issue up to 1 million shares of preferred stock in one or more series or classes and to designate the rights, preferences and privileges of each series or class, which may be greater than the rights of our common stock. It is not possible to state the actual effect of the issuance of any additional shares of preferred stock upon the rights of holders of our common stock until our Board of Directors determines the specific rights of the holders of the preferred stock. However, the effects might include:

- restricting dividends on our common stock;
- diluting the voting power of our common stock;

Explanation of Responses:

- impairing liquidation rights of our common stock; or
- delaying or preventing a change in control of us without further action by our stockholders.

The Board of Directors' authority to issue preferred stock without stockholder approval could make it more difficult for a third-party to acquire control of our company, and could discourage such attempt. We have no present plans to issue any shares of preferred stock.

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The holders of our Series B Preferred are entitled to receive, and we are obligated to pay, cumulative dividends at the rate per share (as a percentage of the stated value per share) of 4% per annum for the first year and thereafter 8%, payable quarterly on March 31, June 30, September 30 and December 31. Dividends are payable in cash or in shares of newly issued common stock, depending on whether we have cash available for lawful payment of dividends and whether we satisfy certain conditions for the alternative to pay the dividends in shares. Each share of Series B Preferred is convertible, at any time at the option of the holder thereof, into that number of our shares of common stock (subject to certain limitations) determined by dividing the Stated Value per share of Series B Preferred by the Conversion Price which is \$0.02 per share. The conversion price of the Series B Preferred is subject to anti-dilution protection upon the happening of certain events such as stock splits as well as certain other issuances below the price at which the Series B Preferred was issued.

Our Series B Preferred generally is non-voting, provided that our holders of Series B Preferred have rights of approval with regard to amendments to our Certificate of Incorporation or to the Certificate of Designation that would adversely affect the rights of our Series B Preferred. Our Series B Preferred provides for a number of negative covenants applicable to us, including restrictions on the amount of our indebtedness and related liens, and restrictions on our use of cash to redeem or to pay dividends with respect to our common stock or other junior securities. In various “triggering event” circumstances set forth in the Series B Certificate of Designation, the holders of our Series B Preferred have rights to demand the redemption of their shares, for cash or for shares of our common stock, depending on the nature of the triggering event, including a change of control.

The holders of our Series C Preferred are entitled to receive, and we are obligated to pay, cumulative dividends at the rate per share (as a percentage of the stated value per share) of 8% per annum, payable quarterly on March 31, June 30, September 30 and December 31. Dividends are payable in cash or in shares of newly issued common stock, depending on whether we have cash available for lawful payment of dividends and whether we satisfy certain conditions for the alternative to pay the dividends in shares. Each share of Series C Preferred is convertible, at any time at the option of the holder thereof, into that number of our shares of common stock (subject to certain limitations) determined by dividing the Stated Value per share of Series C Preferred by the Conversion Price which is \$0.02 per share. The conversion price of the Series C Preferred is subject to anti-dilution protection upon the happening of certain events such as stock splits as well as certain other issuances below the price at which the Series C Preferred was issued.

Our Series C Preferred generally is non-voting, provided that our holders of Series C Preferred have rights of approval with regard to amendments to our Certificate of Incorporation or to the Certificate of Designation that would adversely affect the rights of our Series C Preferred. Our Series C Preferred provides for a number of negative covenants applicable to us, including restrictions on the amount of our indebtedness) and related liens, and restrictions on our use of cash to redeem or to pay dividends with respect to our common stock or other junior securities. In various “triggering event” circumstances set forth in the Series C Certificate of Designation, the holders of our Series C Preferred have rights to demand the redemption of their shares, for cash or for shares of our common stock, depending on the nature of the triggering event, including a change of control.

The holders of our Series D Preferred are entitled to receive, and we are obligated to pay, cumulative dividends at the rate per share (as a percentage of the stated value per share) of 8% per annum, payable quarterly on March 31, June 30, September 30 and December 31. Dividends are payable in cash or in shares of newly issued common stock, depending on whether we have cash available for lawful payment of dividends and whether we satisfy certain conditions for the alternative to pay the dividends in shares. Each share of Series D Preferred is convertible at the option of the holder thereof, commencing upon the earlier of the date that is 180 days after the initial closing (that is, August 14, 2013) or the date two business days after our next stockholder meeting, into that number of shares of our common stock (subject to certain limitations) determined by dividing the Stated Value (which initially was \$1000) per share of Series D Preferred by a \$ conversion price, which is \$0.02 per share. After the initial closing, the securities

purchase agreement permits the holder of the Series D Preferred to exercise a “call” right to purchase additional Series D Preferred in multiple draw downs from time to time until December 31, 2013, subject to certain limits, terms and conditions. Based on the initial Conversion Price, the 150 shares of Series D Preferred issued on the date hereof would be convertible into 1,500,000 shares of common stock. The conversion price of the Series D Preferred is subject to anti-dilution protection upon the happening of certain events such as stock splits as well as certain other issuances below the price at which the Series D Preferred was issued.

Our Series D Preferred generally is non-voting, provided that our holders of Series D Preferred have rights of approval with regard to amendments to our Certificate of Incorporation or to the Certificate of Designation that would adversely affect the rights of our Series C Preferred. Our Series D Preferred provides for a number of negative covenants applicable to us, including restrictions on the amount of our indebtedness and related liens, and restrictions on our use of cash to redeem or to pay dividends with respect to our common stock or other junior securities. In various “triggering event” circumstances set forth in the Series D Certificate of Designation, the holders of our Series D Preferred have rights to demand the redemption of their shares, for cash or for shares of our common stock, depending on the nature of the triggering event, including a change of control.

As of July 17, 2015, we have authorized (i) 2,000 shares of Series A Convertible Preferred Stock, par value \$0.001, (ii) 4,000 shares of Series B 4% Convertible Preferred Stock, par value \$0.001, (iii) 1,175 shares of our Series C 8% Convertible Preferred Stock, par value \$0.001, and (iv) 1,180 shares of our Series D 8% Convertible Preferred Stock, par value \$0.001. All preferred stock has been converted or cancelled and none remain outstanding.

SHARES ELIGIBLE FOR FUTURE SALE

The sale of a substantial amount of our common stock in the public market after this offering, or the perception that such sales may occur, could adversely affect the prevailing market price of our common stock.

Upon the completion of this offering, we will have 550,040,909 shares of common stock outstanding.

Of the shares to be outstanding after the closing of this offering, the shares sold in this offering will not be eligible for resale under Rule 144 of the Securities Act but will be freely tradable without restriction under the Securities Act by reason of this registration statement.

Transfer Agent

Our transfer agent is American Stock Transfer & Trust Company, LLC, 1218 Third Avenue Suite 1700, Seattle, Washington 98101, telephone (206) 682-0811.

EXPERTS

The consolidated financial statements of Andalay Solar, Inc. as of December 31, 2014 and 2013 and for each of the two years in the period ended December 31, 2014 included in this prospectus have been so included in reliance on the report (which contains an explanatory paragraph relating to the Company's ability to continue as a going concern as described in Note 2 to the consolidated financial statements) of Burr Pilger Mayer, Inc., an independent registered public accounting firm, given the authority of such firm as experts in auditing and accounting.

DISCLOSURE OF COMMISSION POSITION ON INDEMNIFICATION
FOR SECURITIES ACT LIABILITIES

Our directors and officers are indemnified as provided by the Delaware General Corporation Law and our Certificate of Incorporation. Section 145 of the Delaware General Corporation Law provides that a director or officer is not individually liable to the corporation or its stockholders or creditors for any damages as a result of any act or failure to act in his capacity as a director or officer unless it is proven that: (1) his act or failure to act constituted a breach of his fiduciary duties as a director or officer; and (2) his breach of those duties involved intentional misconduct, fraud or a knowing violation of law. Our Certificate of Incorporation provides for indemnification of our directors and officers to the fullest extent permitted by Section 145 of the Delaware General Corporation Law.

This provision is intended to afford directors and officers protection against and to limit their potential liability for monetary damages resulting from suits alleging a breach of the duty of care by a director or officer. As a consequence of this provision, stockholders of our company will be unable to recover monetary damages against directors or officers for action taken by them that may constitute negligence or gross negligence in performance of their duties unless such conduct falls within one of the foregoing exceptions. The provision, however, does not alter the applicable standards governing a director's or officer's fiduciary duty and does not eliminate or limit the right of our company or any stockholder to obtain an injunction or any other type of non-monetary relief in the event of a breach of fiduciary duty.

LEGAL MATTERS

The validity of our common stock offered hereby will be passed upon for us by Gracin & Marlow, LLP, New York, New York.

WHERE YOU CAN FIND MORE INFORMATION

We are subject to the informational requirements of the Exchange Act, and file annual and current reports, proxy statements and other information with the Commission. These reports, proxy statements and other information filed by Andalay Solar, Inc. can be read and copied at the Commission's Public Reference Room at 100 F Street, N.W., Washington, D.C. 20549. You may obtain information on the operation of the Public Reference Room by calling the Commission at 1-800-SEC-0330. We will provide to the record holders of our securities a copy of our annual reports containing audited financial statements and such periodic and quarterly reports free of charge upon request.

The Commission also maintains a website that contains reports, proxy statements, information statements and other information located at <http://www.sec.gov>. This prospectus does not contain all the information required to be in the registration statement (including the exhibits), which we have filed with the Commission under the Securities Act and to which reference is made in this prospectus.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of
Andalay Solar, Inc.

We have audited the accompanying consolidated balance sheets of Andalay Solar, Inc. (formerly Westinghouse Solar, Inc.) and its subsidiaries (the "Company") as of December 31, 2014 and 2013, and the related consolidated statements of operations, changes in redeemable convertible preferred stock and stockholders' deficit and cash flows for each of the two years in the period ended December 31, 2014. The Company's management is responsible for these consolidated financial statements. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above, present fairly, in all material respects, the financial position of Andalay Solar, Inc. (formerly Westinghouse Solar, Inc.) and its subsidiaries as of December 31, 2014 and 2013, and the results of their operations and their cash flows for each of the two years in the period ended December 31, 2014 in conformity with accounting principles generally accepted in the United States of America.

The accompanying consolidated financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 2 to the consolidated financial statements, the Company's significant operating losses and negative cash flow from operations raise substantial doubt about its ability to continue as a going concern. The consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

/s/ Burr Pilger Mayer, Inc.

San Jose, California
April 15, 2015

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Andalay Solar, Inc.
Consolidated Balance Sheets

	December 31,	
	2014	2013
Assets		
Current assets:		
Cash	\$ 61,542	\$ 150,081
Accounts receivable, net	118,456	567,523
Other receivables	—	21,378
Inventory	728,372	786,636
Prepaid expenses and other current assets	280,066	317,510
Total current assets	1,188,436	1,843,128
Property and equipment, net	699	13,854
Patents, net	1,131,327	1,244,712
Other assets, net	240,478	363,711
Total assets	\$ 2,560,940	\$ 3,465,405
Liabilities, Redeemable Convertible Preferred Stock and Stockholders' Deficit		
Current liabilities:		
Accounts payable	\$ 3,345,361	\$ 4,199,511
Accrued liabilities	104,229	89,730
Deferred revenue	15,450	—
Accrued warranty	938,466	1,312,918
Credit facility	500,000	500,000
Capital lease obligations – current portion	—	299
Derivative liability – embedded conversion feature	129,598	177,927
Note payable – short-term	109,164	129,839
Convertible notes – short-term	30,000	60,000
Total current liabilities	5,172,268	6,470,224
Convertible notes	343,499	382,084
Total liabilities	5,515,767	6,852,308
Commitments and contingencies (Note 17)		
Series C convertible redeemable preferred stock, \$0.001 par value; 0 and 87 shares issued and outstanding as of December 31, 2014 and 2013, respectively	—	163,998
Series D convertible redeemable preferred stock, \$0.001 par value; 0 and 860 shares issued and outstanding as of December 31, 2014 and 2013, respectively	—	858,565
Stockholders' deficit:		
Series B convertible redeemable preferred stock, \$0.001 par value; 0 and 467 shares issued and outstanding as of December 31, 2014 and 2013, respectively	—	146,224
Common stock, \$0.001 par value; 500,000,000 shares authorized; 279,475,332 and 116,339,293 shares issued and outstanding as of December 31, 2014 and 2013, respectively	279,475	116,339
Additional paid-in capital	82,026,952	78,717,997
Accumulated deficit	(85,261,254)	(83,390,026)

Total stockholders' deficit	(2,954,827)	(4,409,466)
Total liabilities, redeemable convertible preferred stock and stockholders' deficit	\$ 2,560,940	\$ 3,465,405

The accompanying notes are an integral part of these consolidated financial statements.

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Andalay Solar, Inc.

Consolidated Statements of Operations

	Year Ended December 31,	
	2014	2013
Net revenue	\$ 1,288,985	\$ 1,124,836
Cost of goods sold	1,191,390	1,121,612
Gross profit	97,595	3,224
Operating Expenses		
Sales and marketing	366,543	887,305
General and administrative	2,263,086	2,377,703
Total operating expenses	2,629,629	3,265,008
Loss from operations	(2,532,034)	(3,261,784)
Other Income (Expense)		
Interest income (expense), net	(362,955)	(65,031)
Adjustment to the fair value of embedded derivatives	(50,809)	65,962
Adjustment to the fair value of common stock warrants	—	9
Settlement of prior debt owed	769,148	420,000
Total other income, net	355,384	420,940
Loss before provision for income taxes	(2,176,650)	(2,840,844)
Provision for income taxes	—	—
Net loss from continuing operations	(2,176,650)	(2,840,844)
Gain from discontinued operations	324,349	10,797
Net loss	(1,852,301)	(2,830,047)
Preferred stock dividend	(18,927)	(153,305)
Preferred deemed dividend	—	(875,304)
Net loss attributable to common stockholders	\$ (1,871,228)	\$ (3,858,656)
Net loss per common and common equivalent share (basic and diluted) attributable to common shareholders	\$ (0.01)	\$ (0.06)
Weighted average shares used in computing loss per common share: (basic and diluted)	203,814,897	69,170,957

The accompanying notes are an integral part of these consolidated financial statements.

Andalay Solar, Inc.

Consolidated Statements of Changes in Redeemable Convertible Preferred Stock and Stockholders' Deficit

	Series C Convertible Redeemable Preferred Stock		Series D Convertible Redeemable Preferred Stock		Series B Convertible Redeemable Preferred Stock		Common Stock		Additional Paid-in Capital	Accu D
	Number of Shares	Amount	Number of Shares	Amount	Number of Shares	Amount	Number of Shares	Amount		
Balance as of January 1, 2013	800	\$ 983,747	—	\$ —	2,243	\$ 741,171	26,924,643	\$ 26,916	\$ 76,455,063	\$ (79
Issuance of Series C convertible redeemable preferred stock for cash	75	75,000	—	—	—	—	—	—	—	—
Issuance of Series D convertible redeemable preferred stock for cash, net	—	—	950	475,000	—	—	—	—	—	—
Return of Series D convertible redeemable preferred stock	—	—	(200)	(80,123)	—	—	—	—	—	—
Issuance of Series D convertible redeemable preferred stock for payment of financial advisor fees	—	—	230	230,000	—	—	—	—	—	—
Preferred deemed dividend	—	410,227	—	465,077	—	—	—	—	—	—
Conversion of Series B Convertible Redeemable	—	—	—	—	(1,776)	(594,947)	58,277,813	58,278	536,669	

preferred stock to common stock											
Conversion of Series C Convertible Redeemable preferred stock to common stock	(788)	(1,304,976)	—	—	—	—	18,477,766	18,478	1,286,498		
Conversion of Series D Convertible Redeemable preferred stock to common stock	—	—	(120)	(180,010)	—	—	6,000,000	6,000	174,010		
Convertible Redeemable Preferred Stock dividends paid in common stock	—	—	—	—	—	—	4,310,661	4,313	148,992		
Grant of warrant on issuance of convertible note	—	—	—	—	—	—	—	—	53,623		
Placement agent and registration fees and other direct costs	—	—	—	(51,379)	—	—	—	—	(40,602)		
Grants of restricted stock, net of forfeitures and repurchases for employee taxes	—	—	—	—	—	—	2,348,410	2,354	(6,456)		
Stock-based compensation	—	—	—	—	—	—	—	—	110,200		
Net loss	—	—	—	—	—	—	—	—	—		(2)
Balance as of December 31, 2013	87	163,998	860	858,565	467	146,224	116,339,293	116,339	78,717,997		(83)
Issuance of common stock pursuant to registration	—	—	—	—	—	—	44,079,800	44,080	882,510		

statement										
Issuance of common stock upon conversion of note payable	—	—	—	—	—	—	50,439,751	50,439	957,880	
Conversion of Series B Convertible Redeemable preferred stock to common stock	—	—	—	—	(467)	(146,224)	21,020,015	21,020	125,204	
Conversion of Series C Convertible Redeemable preferred stock to common stock	(87)	(163,998)	—	—	—	—	4,333,350	4,333	159,665	
Conversion of Series D Convertible Redeemable preferred stock to common stock	—	—	(860)	(858,565)	—	—	43,000,000	43,000	815,565	
Convertible Redeemable Preferred Stock dividends paid in common stock	—	—	—	—	—	—	643,520	644	18,283	
Convertible note embedded derivative and warrants, accretion of note to face value	—	—	—	—	—	—	—	—	—	170,767
Placement agent and registration fees and other direct costs	—	—	—	—	—	—	—	—	—	(36,618)
Shares repurchased for employee taxes	—	—	—	—	—	—	(380,397)	(380)	(8,312)	

Explanation of Responses:

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Stock-based compensation	—	—	—	—	—	—	—	—	224,011
Net loss	—	—	—	—	—	—	—	—	— (1)
Balance as of December 31, 2014	—\$	—	—\$	—	—\$	—279,475,332	\$ 279,475	\$ 82,026,952	\$(85)

The accompanying notes are an integral part of these consolidated financial statements.

Andalay Solar, Inc.

Consolidated Statements of Cash Flows

	Year Ended December 31,	
	2014	2013
Cash flows from operating activities		
Net loss	\$ (1,852,301)	\$ (2,830,047)
Adjustments to reconcile net loss to net cash used in operations:		
Depreciation	13,155	33,023
Amortization of patents	113,385	113,071
Bad debt expense	36,763	92,224
Adjustment to the fair value of embedded derivatives	50,809	(65,962)
Accretion of interest on convertible notes	168,708	21,889
Unrealized gain on fair value adjustment of common stock warrants	—	(9)
Stock-based compensation expense	224,011	110,200
Non-cash settlement of prior debt owed	(769,148)	—
Changes in assets and liabilities:		
Accounts receivable	412,304	(293,902)
Other receivables	21,378	100,612
Inventory	58,264	209,077
Prepaid expenses and other current assets	158,544	246,669
Other assets	123,233	1,706
Accounts payable	324,998	1,159,974
Accrued liabilities and accrued warranty	(276,657)	(461,100)
Deferred revenue	15,450	—
Net cash used in operating activities	(1,177,104)	(1,562,575)
Cash flows from financing activities		
Borrowing on long-term debt	600,000	650,000
Repayment of notes payable	(142,416)	(14,232)
Borrowing on line of credit, net	—	500,000
Repayments on capital lease obligations	(299)	(4,414)
Proceeds from securities purchase agreement	676,590	550,000
Payment of placement agent and registration fees and other direct costs	(36,618)	(91,981)
Employee taxes paid for vesting of restricted stock	(8,692)	(4,102)
Net cash provided by financing activities	1,088,565	1,585,271
Net (decrease) increase in cash	(88,539)	22,696
Cash		
Beginning of year	150,081	127,385
End of year	\$ 61,542	\$ 150,081

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Supplemental cash flows disclosures:

Cash paid during the period for interest	\$ 57,580	\$ 6,759
Supplemental disclosure of non-cash financing activity:		
Embedded derivatives on convertible note issuances	\$ 122,630	\$ 243,889
Grant of warrant on issuance of convertible note	\$ 170,767	\$ 53,623
Preferred deemed dividend	\$ —	\$ 875,304
Conversion of preferred stock to common stock	\$ 1,168,787	\$ 2,079,933
Conversion of convertible note to common stock	\$ 786,551	\$ —
Preferred stock dividends paid in common stock	\$ 18,927	\$ 153,305
Return of Series D convertible preferred stock	\$ —	\$ 80,123
Note payable obtained to finance prepaid insurance	\$ 121,100	\$ 144,071
Preferred stock issued for payment of financial advisor fees	\$ —	\$ 230,000
Note payable issued as payment of financial advisor fees	\$ 160,000	\$ 60,000
Common stock issued to settle claim	\$ 250,000	\$ —
Embedded derivative converted to equity	\$ 221,768	\$ —

The accompanying notes are an integral part of these consolidated financial statements.

Andalay Solar, Inc.
Notes to Consolidated Financial Statements
December 31, 2014 and 2013

1. Description of Business

Andalay Solar, Inc. and its subsidiaries (Andalay Solar, the Company, we, us or our) is a designer and manufacturer of integrated solar power systems and solar panels with integrated microinverters (which we call AC solar panels). We design, market and sell these solar power systems to solar installers and do-it-yourself customers in the United States, Canada, the Caribbean and South America through distribution partnerships, our dealer network and retail outlets. Our products are designed for use in solar power systems for residential and commercial rooftop customers. Prior to September 2010, we were also in the solar power installation business, but decided to exit that business. Recently we have re-entered the solar power installation business.

In September 2007, we introduced our “plug and play” solar panel technology (under the brand name “Andalay”), which we believe significantly reduces the installation time and costs, and provides superior reliability and aesthetics, when compared to other solar panel mounting products and technology. Our panel technology offers the following features: (i) mounts closer to the roof with less space in between panels; (ii) no unsightly racks underneath or beside panels; (iii) built-in wiring connections; (iv) approximately 70% fewer roof-assembled parts and approximately 50% less roof-top labor required; (v) approximately 25% fewer roof attachment points; (vi) complete compliance with the National Electric Code and UL wiring and grounding requirements. We have seven U.S. patents (Patent No. 7,406,800, Patent No. 7,832,157, Patent No. 7,866,098, Patent No. 7,987,641, Patent No. 8,505,248, Patent No. 8,813,460, and Patent No. 8,938,919) that cover key aspects of our Andalay solar panel technology, as well as U.S. Trademark No. 348565 3 for registration of the mark “Andalay Solar.” In addition to these U.S. patents, we have eight foreign patents. Currently, we have 15 issued patents and nine other pending U.S. and foreign patent applications that cover the Andalay technology working their way through the United States Patent and Trademark Office (“USPTO”) and foreign patent offices.

In February 2009, we began our strategic relationship with Enphase, a leading manufacturer of microinverters, to develop and market solar panel systems with ordinary AC house current output instead of high voltage DC output. We introduced Andalay AC panel products and began offering them to our customers in the second quarter of 2009. Andalay AC panels cost less to install, are safer, and generally provide higher energy output than ordinary DC panels. Andalay AC panels deliver 5-25% more energy compared to ordinary panels, produce safe household AC power, and have built-in panel level monitoring, racking, wiring, grounding and microinverters. With 80% fewer parts and 5 – 25% better performance than ordinary DC panels, we believe Andalay AC panels are an ideal solution for solar installers and do-it-yourself customers.

On May 7, 2012, we announced the execution of an agreement and plan of merger with CBD Energy Limited, an Australian corporation (CBD), which contemplated a merger in which CBD would become our parent company. The targeted completion of the merger was repeatedly delayed and on July 18, 2013 we terminated the merger. During such merger delays, our supply relationships had been disrupted, leading to a significant decline in our revenue and the implementation of significant cost reductions, including the lay-off of employees during the time we pursued the merger. Since the termination of the merger, we have been committed to focus our attention on rebuilding our core business, expanding our current product offering and exploring strategic opportunities.

In September 2013, we entered into a supply agreement for assembly of our proprietary modules with Tianwei New Energy Co, Ltd., (Tianwei) a panel supplier located in China. We began receiving initial shipments from Tianwei in February 2014 but ended our relationship in June 2014.

On July 16, 2014, we entered into an agreement for supply of solar photovoltaic (“PV”) modules with Auxin Solar Inc. These modules are assembled in the United States and we began distributing these panels from our new supplier in December 2014.

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Prior to September 2010, we were also in the solar power system installation business and we had completed over 4,300 solar power installations for customers in California, New York, New Jersey, Pennsylvania, Colorado and Connecticut since the commencement of our operations in 2001. In early 2009, we closed our non-California offices on the east coast and in Colorado and began distributing our solar power systems to customers outside of California. In September 2010, we made the strategic decision to exit our California solar panel installation business and expand our solar panel distribution network to dealers and other installers in California, by far the largest solar market in the United States. However, we recently made the decision to re-enter the solar panel installation business on a limited basis. Our business is now focused on design and manufacturing activities, and sales of our solar power systems to solar installers, trade workers and retailers through distribution partnerships, our dealer network and retail home improvement outlets as well as installation of our panels.

We were incorporated in February 2001 as Akeena Solar, Inc. in the State of California and elected at that time to be taxed as an S corporation. During June 2006, we reincorporated in the State of Delaware and became a C corporation. On August 11, 2006, we entered into a reverse merger transaction with Fairview Energy Corporation, Inc. (“Fairview”). Pursuant to the merger, our stockholders received one share of Fairview common stock for each issued and outstanding share of our common stock. Our common shares were also adjusted from \$0.01 par value to \$0.001 par value at the time of the Merger. On May 17, 2010, we entered into an exclusive worldwide license agreement with Westinghouse, Inc, which permitted us to manufacture, distribute and market solar panels under the Westinghouse name and in connection therewith, on April 6, 2011, we changed our name to Westinghouse Solar, Inc. On April 13, 2011, we effected a reverse split of our common stock at a ratio of 1 – for – 4. On August 23, 2013, the license agreement with Westinghouse, Inc. was terminated and on September 19, 2013, we changed our name to our current name, Andalay Solar, Inc. and increased our number of authorized shares of common stock to 500,000,000.

2. Summary of Significant Accounting Policies

Liquidity and Financial Position

We currently face challenges meeting the working capital needs of our business. Our primary requirements for working capital are to fund purchases for solar panels and microinverters, and to cover our payroll and lease expenses. We have incurred net losses and negative cash flows from operations for each of the years ended December 31, 2014 and 2013. During recent years, we have undertaken several equity and debt financing transactions to provide the capital needed to sustain our business. We have dramatically reduced our headcount and other variable expenses. As of December 31, 2014, we had approximately \$62,000 in cash on hand. We intend to address ongoing working capital needs through sales of remaining inventory, along with raising additional debt and equity financing. In January 2013, our board of directors approved actions to dramatically reduce our variable operating costs, including a 12 person employee headcount reduction effective January 15, 2013, for the period through the anticipated merger closing with CBD, which was terminated in July 2013. No restructuring charges or severance payments were incurred. Our revenue levels remain difficult to predict, and as we anticipate we will continue to sustain losses in the near term, we cannot assure investors that we will be successful in reaching break-even.

During 2012, because of our cash position and liquidity constraints, we were late in making payments to both of our former panel suppliers, Suntech and Lightway. We currently have no unshipped orders from these suppliers. In September 2013, we entered into a supply agreement for assembly of our proprietary modules with Tianwei New Energy Co, Ltd., a panel supplier located in China. We began receiving product from Tianwei in February 2014 and stopped as of June 2014. In July 2014, we entered into a supply agreement for assembly of our proprietary modules with Auxin Solar, Inc., a panel supplier located in the United States. In December 2014, we began distributing panels from our new supplier. Although we believe we can find alternative suppliers for solar panels manufactured to our specifications, our operations would be disrupted unless we are able to rapidly secure alternative sources of supply, our inventory and revenue could diminish significantly, causing disruption to our operations.

The accompanying consolidated financial statements have been prepared assuming we will continue as a going concern. Our significant operating losses, negative cash flow from operations, and challenges in rapidly securing alternative sources of supply for solar panels, raise substantial uncertainty about our ability to continue as a going concern. The accompanying financial statements do not include any adjustments that might result from the outcome of this uncertainty, and contemplate the realization of assets and the settlement of liabilities and commitments in the normal course of business. There can be no assurance that we will be able to raise additional funds on commercially reasonable terms, if at all. There is uncertainty to our anticipated revenue levels and to the timing of cash receipts, which are needed to support our operations. It also worsens the market conditions for seeking equity and debt financing. We currently anticipate that we will retain all of our earnings, if any, for development of our business and do not anticipate paying any cash dividends on common stock in the foreseeable future.

Convertible Notes payable

On August 30, 2013, we entered into a securities purchase agreement with Alpha Capital Anstalt (“Alpha Capital”) relating to the sale and issuance of a convertible note in the principal amount of \$200,000 that matures August 29, 2015 (the "Convertible Note"). Subsequently, on November 25, 2013 and December 19, 2013, we entered into additional securities purchase agreements with Alpha Capital relating to the sale and issuance of convertible notes in the principal amount of \$200,000 and \$250,000, respectively, which mature on November 25, 2015 and December 19, 2015. On January 27, 2014, we issued a convertible note in the principal amount of \$100,000 that matures on January 27, 2016 under the Securities Purchase Agreement we entered into with Alpha Capital on December 19, 2013. In connection with the issuance of the December 19, 2013 convertible note, we also issued 6,250,000 warrants to purchase shares of our common stock at a price of \$0.02 per share. On February 25, 2014, we entered into a Securities Purchase Agreement with the Alpha Capital related to the sale and issuance of a convertible note in the principal amount of \$200,000 that matures on February 25, 2016. In connection with the issuance of the February 25, 2014 convertible note, we issued 5,000,000 warrants to purchase shares of our common stock at a price of \$0.02 per share. On March 18, 2014, we entered into a Securities Purchase Agreement with the Alpha Capital related to the sale and issuance of a convertible note in the principal amount of \$300,000 that matures on March 18, 2016. In connection with the March 18, 2014 convertible note, we issued a five-year warrant to purchase 7,500,000 shares of our common stock at an exercise price of \$.02 per share. Each of the Convertible Notes bear interest at the rate of 8% per annum compounded annually, are payable at maturity and the principal and interest outstanding under the convertible notes are convertible into shares of our common stock, at any time after issuance, at the option of the purchaser, at a conversion price equal to \$0.02 per share, subject to adjustment upon the happening of certain events, including stock dividends, stock splits and the issuance of common stock equivalents at a price below the conversion price. Subject to our fulfilling certain conditions, including beneficial ownership limits, the convertible notes are subject to a mandatory conversion if the closing price of our common stock for any 20 consecutive days commencing six months after the issue date of the convertible notes equal or exceeds \$0.04 per share. Unless waived in writing by the purchaser, no conversion of the convertible notes can be effected to the extent that as a result of such conversion the purchaser would beneficially own more than 9.99% in the aggregate of our issued and outstanding common stock immediately after giving effect to the issuance of common stock upon conversion.

We have the option of repaying the outstanding principal amount of the convertible notes, in whole or in part, by paying the purchaser a sum of money equal to one hundred and twenty percent (120%) of the principal together with accrued but unpaid interest upon 30 days' notice, subject to certain beneficial ownership limits. For so long as we have any obligation under the convertible notes, we have agreed to certain restrictions regarding, among other things, incurrence of additional debt, liens, amendments to charter documents, repurchase of stock, payment of cash dividends, affiliated transactions. We are also prohibited from entering into certain variable priced agreements until the convertible notes are repaid in full.

Because of certain down-round protection in the conversion rate of the convertible notes, we determined that the derivative liability related to the embedded conversion feature met the criteria for bifurcation. Accordingly, we recognized an aggregate liability of \$123,000 on the three issuance dates during the year ended December 31, 2014. This was in addition to the carrying value of the derivative liability on three previously recorded derivatives of \$178,000. The derivative liability is carried at fair value with changes in the fair value reflected in the "Adjustment to the fair value of embedded derivatives" line item of our condensed consolidated statements of operations. We recognized a non-cash benefit for the year ended December 31, 2014 of \$51,000 on a total of six convertible notes.

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In addition, the relative fair value of the warrants issued in the December 2013 convertible note issuance of \$250,000, were allocated to additional paid-in capital. Such value was determined assuming volatility of 149.1%, a risk free interest rate of 0.7% and an expected term of 4.1 years. The resulting debt discount from the derivative liability and warrant issuance of \$109,000 is being accreted to interest using the effective interest method. The relative fair value of the warrants issued in the February 2014 convertible note issuance of \$200,000, were allocated to additional paid-in capital. Such value was determined assuming volatility of 169.1, a risk free interest rate of 0.7% and an expected term of 4.1 years. The resulting debt discount from the derivative liability and warrant issuance of \$101,000 is being accreted to interest using the effective interest method. The relative fair value of the warrants issued in the March 2014 convertible note issuance of \$300,000, were allocated to additional paid-in capital. Such value was determined assuming volatility of 168.8%, a risk free interest rate of 0.8% and an expected term of 4.1 years. The resulting debt discount from the derivative liability and warrant issuance of \$154,000 is being accreted to interest using the effective interest method.

On November 1 and December 1, 2013, and on January 1, February 1 and March 1, 2014, we issued convertible notes to our financial advisory firm in the principal amount of \$30,000 each for a total of \$150,000, which mature on October 31, November 30 and December 31, 2014, and on January 31 and February 28, 2015, respectively. On April 1, May 1 and June 1, 2014, we issued convertible notes to our financial advisory firm in the principal amount of \$20,000 each, for a total of \$60,000, which mature on March 31, April 30 and May 31, 2015, respectively. On July 1, 2014, we issued convertible notes to our financial advisory firm in the principal amount of \$10,000, which matures on June 30, 2015. Each of the Convertible Notes bear interest at the rate of 8% per annum compounded annually, are payable at maturity and the principal and interest outstanding under the convertible notes are convertible into shares of our common stock, at any time after issuance, at the option of the purchaser, at a conversion price equal to \$0.02 per share. Unless waived in writing by the purchaser, no conversion of the convertible notes can be effected to the extent that as a result of such conversion the purchaser would beneficially own more than 9.99% in the aggregate of our issued and outstanding common stock immediately after giving effect to the issuance of common stock upon conversion. During 2014, convertible notes in the principal amount of approximately \$940,000, along with accrued interest of \$68,319, were converted into 50,439,751 shares of our common stock.

Line of credit

On September 30, 2013, we entered into a loan and security agreement with Alpha Capital Anstalt and Collateral Services, LLC to provide financing, on a discretionary basis, for one year, against our accounts receivable and inventory. The maximum amount that can be borrowed under the Agreement is \$500,000. We have the right to borrow up to 80% of our eligible accounts receivable, not in excess of \$200,000, 50% of the value of our raw materials in inventory, 65% of our finished goods inventory and 95% of cash, but not in the aggregate amount in excess of \$300,000. The advances are secured by a lien on all of our assets. All advances under the agreement bear interest at a per annum rate of 12% and monthly interest shall be a minimum of \$500. At the time of initial funding we paid a loan fee of 50 shares of our Series D Preferred Shares to the lender, in addition to other payments for legal fees. In addition, we paid the collateral agent an initial fee of \$5,000 and have agreed to pay an administrative fee to the collateral agent of 0.5% per month of the daily balance during the preceding month or \$500 whichever is less. In the event that of a prepayment, we are obligated to pay a prepayment fee in an amount equal to one-half of one percent (0.5%) of \$500,000. On September 30, 2013, we requested and received an initial borrowing under the Agreement totaling \$350,000. Subsequently, on October 21, 2013, we requested and received an additional \$100,000 and on November 20, 2013, we requested and received an additional \$50,000. As of December 31, 2014, the balance outstanding under our line of credit was \$500,000. On February 27, 2015, we agreed to extend the term of the agreement for one year, and to exchange the \$500,000 plus interest owing under the agreement for a one year, 8%, convertible note. We are no longer able to make borrowings under the line of credit agreement.

Cash and Cash Equivalents

Explanation of Responses:

We consider all highly liquid investments with maturities of three months or less, when purchased, to be cash equivalents. At certain times, such amounts exceed FDIC insurance limits. We have not experienced any losses on these investments. As of December 31, 2014 and 2013, we had no cash equivalents.

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Accounts Receivable

Accounts receivable consist of trade receivables. We regularly evaluate the collectability of our accounts receivable. An allowance for doubtful accounts is maintained for estimated credit losses. We consider a number of factors when estimating credit losses, including the aging of a customer's account, creditworthiness of specific customers, historical trends and other information.

Inventory

Inventory is stated at the lower of cost (on an average basis) or market value. We determine cost based on the weighted-average purchase price and include both the costs of acquisition and the shipping costs in inventory. We regularly review the cost of inventory against its estimated market value and record a lower of cost or market write-down to cost of goods sold, if any inventory has a cost in excess of estimated market value.

Property and Equipment

Property and equipment are stated at cost less accumulated depreciation and amortization. Depreciation and amortization are provided for using the straight-line method over the estimated useful lives of the respective assets.

Estimated useful lives are as follows:

Category	Useful Lives
Office Equipment	2-5 years
Vehicles	3-5 years
Leasehold Improvements	2 years

Maintenance and repairs are expensed as incurred. Expenditures for significant renewals or betterments are capitalized. Upon disposition, the cost and related accumulated depreciation are removed from the accounts and the resulting gain or loss is reflected in current operations.

Long-Lived Assets

We review long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying value of a long-lived asset may not be recoverable. We periodically evaluate whether events and circumstances have occurred that may warrant revision of the estimated useful lives of our long-lived assets or whether the remaining balance of long-lived assets should be evaluated for possible impairment. We do not believe that there were any indicators of impairment that would require an adjustment to such assets or their estimated periods of recovery at December 31, 2014 and 2013.

Patent Costs

We capitalize external legal costs and filing fees associated with obtaining or defending our patents. Upon issuance of new patents or successful defense of existing patents, we amortize these costs using the straight line method over the shorter of the legal life of the patent or its economic life. We believe the remaining useful life we assign to these patents, approximately 10 years as of December 31, 2014, are reasonable. We periodically review our patents to determine whether any such cost have been impaired and are no longer being used. To the extent we are no longer using certain patents, the associated costs will be written off at that time.

Costs associated with patents currently held are approximately \$1.1 million, net of approximately \$314,000 of accumulated amortization, are included in patents, net as of December 31, 2014, and are being amortized over the estimated useful life, which was determined to be seventeen years. Amortization expense of patents was approximately \$113,000 in each of the years ended December 31, 2014 and 2013. Estimated amortization expense of patents for the five years subsequent to December 31, 2013, is approximately \$113,000 per year. Capitalized filing fees associated with obtaining new patents not yet issued and defense of existing patents (not yet resolved) of approximately \$141,000 are included in other assets as December 31, 2014.

Discontinued Operations

Discontinued operations are presented and accounted for in accordance with Accounting Standards Codification (ASC) 360, "Impairment or Disposal of Long-Lived Assets," (ASC 360). When a qualifying component of the Company is disposed of or has been classified as held for sale, the operating results of that component are removed from continuing operations for all periods presented and displayed as discontinued operations if: (a) elimination of the component's operations and cash flows from the Company's ongoing operations has occurred (or will occur) and (b) significant continuing involvement by the Company in the component's operations does not exist after the disposal transaction.

On September 10, 2010, we announced that we were exiting the solar panel installation business. The exit from the installation business was essentially completed at the end of the fourth quarter of 2010. The exit from the installation business was therefore classified as discontinued operations for all periods presented under the requirements of ASC 360.

We re-entered the residential and commercial installation business in the fourth quarter 2014. As a result of re-entering the installation business, we reclassified our discontinued operations into continuing operations.

Reclassifications

Certain prior year amounts have been reclassified for consistency with the current period presentation. These reclassifications had no effect on the reported results of operations.

Manufacturer and Installation Warranties

The manufacturer directly warrants the solar panels and inverters for a range from 15 to 25 years. We warrant the balance of system components of our products against defects in material and workmanship for five years. We assist our customers in the event of a claim under the manufacturer warranty to replace a defective solar panel or inverter. The warranty liability for the material and the workmanship of the balance of system components of approximately \$371,000 as of December 31, 2014 and \$345,000 as of December 31, 2013, is included within "Accrued warranty" in the accompanying consolidated balance sheets.

The liability for our manufacturing warranty consists of the following:

	Years Ended	
	2014	2013
Beginning accrued warranty balance	\$ 1,312,918	\$ 1,372,342
Reduction for labor payments and claims made under the warranty	(75,966)	(79,134)
Accruals related to warranties issued during the period	25,863	19,710
Adjustment to warranty liability for discontinued operations	(324,349)	—
Ending accrued warranty balance	\$ 938,466	\$ 1,312,918

We previously recorded a provision for warranty liability related to our discontinued installation operations. We provided for a 5-year or a 10-year warranty on the installation of a system and all equipment and incidental supplies other than solar panels and inverters that are covered under the manufacturer warranty. During the year ended December 31, 2014, we re-evaluated our warranty liability related to our discontinued installation operations right before and in conjunction with re-entering the installation operations, we reduced the liability by approximately \$324,000. This reduction to the liabilities for discontinued operations was recorded as a gain from operations of discontinued operations. The remaining warranty liability related to our previously discontinued operations was reclassified into current liabilities and has been included in "Accrued warranty." Defective solar panels or inverters are covered under the manufacturer warranty. In the event that a panel or inverter needs to be replaced, we will replace the defective item within the manufacturer's warranty period (between 5-25 years).

Fair Value of Financial Instruments

The carrying values reported for cash equivalents, accounts receivable, accounts payable, accrued liabilities and the outstanding credit facility approximated their respective fair values at each balance sheet date due to the short-term maturity of these financial instruments.

Revenue Recognition

Revenue from sales of products is recognized when: (1) persuasive evidence of an arrangement exists, (2) delivery has occurred or services have been rendered, (3) the sale price is fixed or determinable, and (4) collection of the related receivable is reasonably assured. We recognize revenue when the solar power systems are shipped to the customer. Revenue from installation of a system is recognized when (1) persuasive evidence of an arrangement exists, (2) delivery has occurred or services have been rendered, (3) the sales price is fixed or determinable, and (4) collection of the related receivable is reasonably assured. In general, we recognize revenue upon completion of a system installation for residential installations and we recognize revenue under the percentage-of-completion method for commercial installations. Revenue recognition methods for revenue streams that fall under other categories are determined based on facts and circumstances.

Stock-based Compensation

We apply the fair value method under Accounting Standards Codification (ASC) 718 in accounting for our 2001 Stock Option Plan and our 2006 Stock Incentive Plan. Under ASC 718, compensation cost is measured at the grant date based on the fair value of the equity instruments awarded and is recognized over the period during which an employee is required to provide service in exchange for the award, or the requisite service period, which is usually the vesting period. The fair value of the equity award granted is estimated on the date of the grant.

Advertising

We expense advertising costs as incurred. Advertising expense, included in "Sales and marketing expenses," for the years ended December 31, 2014 and 2013, was approximately \$15,000 and \$16,000, respectively.

Research and Development Costs

Research and development expenses, which include the cost of activities that are useful in developing new products, processes or techniques, as well as expenses for activities that may significantly improve existing products or processes are expensed as incurred. In the years ended December 31, 2014 and 2013, we expensed approximately \$178,000 and \$243,000, respectively, in costs related to research and development activities that are included under general and administrative expenses on the consolidated statements of operations.

Shipping and Handling Costs

Shipping and handling costs associated with inbound freight are included in cost of inventory and expensed as cost of goods sold when the related inventory is sold.

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Income Taxes

Deferred income taxes arise from timing differences resulting from income and expense items reported for financial accounting and tax purposes in different periods. A deferred tax asset valuation allowance is recorded when it is more likely than not that deferred tax assets will not be realized. Utilization of net operating loss carryforwards may be subject to a substantial annual limitation due to ownership change limitations provided by the Internal Revenue Code. The annual limitation may result in the expiration of net operating loss carryforwards before utilization. We apply the provisions of ASC 740, formerly FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes" (FIN 48). We recognize the financial statement benefit of a tax position only after determining that the relevant tax authority would more likely than not sustain the position following an audit. For tax positions meeting this standard, the amount recognized in the financial statements is the largest benefit that has a greater than 50 percent likelihood of being realized upon ultimate settlement with the relevant tax authority.

Earnings Per Share

We follow Accounting Standards Codification (ASC) 260 (ASC 260), "Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities" (the "Staff Position"), which states that unvested share-based payment awards that contain non-forfeitable rights to dividends or dividend equivalents are considered participating securities and shall be included in the computation of net income (loss) per share pursuant to the two-class method described in ASC, Earnings Per Share.

In accordance with the Staff Position, basic net income (loss) per share is computed by dividing net income (loss), excluding net income (loss) attributable to participating securities, by the weighted average number of shares outstanding less the weighted average unvested restricted shares outstanding. Diluted net income (loss) per share is computed by dividing net income (loss), excluding net income (loss) attributable to participating securities, by the denominator for basic net income (loss) per share and any dilutive effects of stock options, restricted stock, convertible notes and warrants.

The following table sets forth the computation of basic and diluted net loss per share:

	Year Ended December 31,	
	2014	2013
Basic:		
Numerator:		
Net loss	\$ (1,852,301)	\$ (2,830,047)
Preferred deemed dividend and preferred stock dividend	(18,927)	(1,028,609)
Less: Net loss allocated to participating securities	6,005	12,503
	\$ (1,865,223)	\$ (3,846,153)
Denominator:		
Weighted-average shares outstanding	204,471,018	69,477,915
Weighted-average unvested restricted shares outstanding	(656,121)	(306,958)
Denominator for basic net loss per share	203,814,897	69,170,957
Basic net loss per share attributable to common stockholders	\$ (0.01)	\$ (0.06)

The following table sets forth potential shares of common stock at the end of each period presented that are not included in the calculation of diluted net loss per share because to do so would be anti-dilutive:

	December 31, 2014	December 31, 2013
Stock options outstanding	37,034,483	5,368,233
Unvested restricted stock	7,186	1,890,952
Warrants to purchase common stock	22,148,045	9,648,045
Preferred stock convertible into common stock		— 68,353,582

Segment Reporting

Operating segments are components of an enterprise for which separate financial information is available and is evaluated regularly by management in deciding how to allocate resources and in assessing performance. We are engaged in two business segments; (i) we sell our AC solar panels to solar installers, trade workers and do-it-yourself customers through distribution partnerships, our dealer network and retail outlets, and (ii) we market, sell, design and install systems for residential and commercial customers. Operating segments are components of an enterprise for which separate financial information is available and is evaluated regularly by management in deciding how to allocate resources and in assessing performance. We re-entered the residential and commercial installation business in the fourth quarter 2014, and we do not report separate segment information because these sales are not material for the year ended December 31, 2014.

Use of Estimates

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

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of Andalay Solar and Fairview, pursuant to the Merger as described in Note 1. We also have two wholly-owned subsidiaries as of December 31, 2014 and 2013. Akeena Corp. is a wholly-owned subsidiaries of Andalay Solar, Inc. All inter-company accounts have been eliminated in consolidation.

Recent Accounting Pronouncements

In April 2014, the FASB issued Accounting Standards Update (“ASU”) 2014-08, "Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity" (ASU 2014-08). ASU 2014-08 changes the criteria for reporting discontinued operations by requiring that in order for a disposal to qualify as a discontinued operation, the disposal must represent a strategic shift that has (or will have) a major effect on the entity's operations and financial results. ASU 2014-08 also requires additional disclosures both for discontinued operations and individually significant components of an entity that do not qualify as discontinued operations. ASU 2014-08 is effective for annual and interim periods beginning on or after December 15, 2014, with early adoption permitted. We adopted the provisions of ASU 2014-08 and such adoption did not have a material impact on our consolidated financial statements.

In May 2014, as part of its ongoing efforts to assist in the convergence of U.S. GAAP and International Financial Reporting Standards (“IFRS”), the FASB issued ASU 2014-09, “Revenue from Contracts with Customers.” The new guidance sets forth a new five-step revenue recognition model which replaces the prior revenue recognition guidance in its entirety and is intended to eliminate numerous industry-specific pieces of revenue recognition guidance that have historically existed in U.S. GAAP. The underlying principle of the new standard is that a business or other organization will recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects what it expects in exchange for the goods or services. The standard also requires more detailed disclosures and provides additional guidance for transactions that were not addressed completely in the prior accounting guidance. The ASU provides alternative methods of initial adoption and is effective for annual and interim periods beginning after December 15, 2016. We are currently evaluating the impact that this standard will have on our consolidated financial statements.

In June 2014, the FASB issued ASU No. 2014-12, "Compensation – Stock Compensation: Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could be Achieved After a Requisite Service Period" ("ASU 2014-12") Companies commonly issue share-based payment awards that require a specific performance target to be achieved in order for employees to become eligible to vest in the awards. ASU 2014-12 requires that a performance target that affects vesting and that could be achieved after the requisite service period should be treated as a performance condition. The performance target should not be reflected in estimating the grant date fair value of the award. Compensation cost should be recognized in the period in which it becomes probable that the performance target will be achieved. ASU 2014-12 will be effective for the Company's fiscal years beginning fiscal 2016 and interim reporting periods within that year, using either the retrospective or prospective transition method. Early adoption is permitted. We are currently evaluating the effect of the adoption of this guidance on the condensed consolidated financial statements.

In August 2014, the FASB issued ASU No. 2014-15, "Presentation of Financial Statements – Going Concern: Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern" ("ASU 2014-15"), to provide guidance on management's responsibility in evaluating whether there is substantial doubt about a company's ability to continue as a going concern and to provide related footnote disclosures. ASU 2014-15 is effective for the annual period ending after December 15, 2016, and for annual periods and interim periods thereafter. Since ASU 2014-15 only impacts financial statement disclosure requirements regarding whether there is substantial doubt about an entity's ability to continue as a going concern, we do not expect its adoption to have an impact on our consolidated financial statements.

3. Discontinued Operations

On September 10, 2010, we announced that we were exiting the solar panel installation business and we were expanding our distribution business to include sales of our Andalay Solar Power Systems directly to dealers in California. The exit from the installation business was essentially completed by the end of 2010. As a result of the

decision to exit the California installation business we recorded a restructuring charge totaling approximately \$3.0 million for the year ended December 31, 2010, the majority of which were non-cash charges. This restructuring charge was comprised primarily of (i) one-time severance costs of \$765,000 related to headcount reductions paid primarily in shares of our common stock, (ii) inventory write downs of \$948,000, (iii) lease accelerations and the write off of leasehold improvements of \$307,000, (iv) goodwill impairment of \$299,000, (v) vehicle, furniture and fixtures and computer equipment write downs of \$290,000 and (vi) other prepaid costs write-downs of \$367,000. During the year ended December 31, 2010, we recorded a loss from discontinued operations of \$6.5 million.

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During the year ended December 31, 2014, we re-evaluated our warranty liability related to our discontinued installation operations right before and in conjunction with re-entering the installation operations, and reduced the liability by approximately \$324,000. This reduction to the liabilities for discontinued operations was recorded as a gain from operations of discontinued operations. The remaining warranty liability related to our previously discontinued operations was reclassified into current liabilities and has been included in "Accrued warranty."

We entered into a Supply and Warranty Agreement and Master Assignment Agreement with Real Goods Solar, Inc. (Real Goods), pursuant to which Real Goods has agreed to perform certain warranty work. The terms of the agreement provide that an escrow account be established as a source of funds from which to satisfy our obligation to pay Real Goods for its fees and reimburse it for its expenses for this warranty work. In March 2011, we entered into an Escrow Agreement with Real Goods and deposited \$200,000 into an escrow account. The amount is reflected in other assets in the consolidated balance sheets. The escrow deposit will be released to us in the amount of \$40,000, or one-fifth of the remaining escrow funds, per year after each of the fifth through the ninth anniversary of the escrow agreement. In December 2014, \$110,000 of the funds in escrow were returned by Real Goods.

4. Accounts Receivable

Accounts receivable consists of the following:

	December 31, 2014	December 31, 2013
Trade accounts	\$ 154,172	\$ 575,375
Less: Allowance for bad debts	(24,882)	(2,899)
Less: Allowance for returns	(10,834)	(4,953)
	\$ 118,456	\$ 567,523

The following table summarizes the allowance for doubtful accounts as of December 31, 2014 and 2013:

	Balance as of Beginning of Period	Provisions, net	Write-Off	Balance as of End of Period
Year ended December 31, 2014	\$ 2,899	\$ 36,763	\$ (14,780)	\$ 24,882
Year ended December 31, 2013	\$ 108,750	\$ 92,224	\$ (198,075)	\$ 2,899

5. Inventory

Inventory consists of the following:

	December 31, 2014	December 31, 2013
Finished goods	\$ 669,706	\$ 654,970
Work in process	58,666	131,666
	\$ 728,372	\$ 786,636

6. Prepaid expenses and other current assets

Prepaid expenses and other current assets consist of the following:

	December 31, 2014	December 31, 2013
Prepaid insurance	\$ 116,243	\$ 152,812
Prepaid - other	46,471	68,906
Vendor deposits	117,352	95,792
	\$ 280,066	\$ 317,510

7. Property and Equipment, Net

Property and equipment, net consist of the following:

	December 31, 2014	December 31, 2013
Office equipment	\$ 436,051	\$ 436,051
Leasehold improvements	123,278	123,278
Vehicles	17,992	17,992
	577,321	577,321
Less: Accumulated depreciation and amortization	(576,622)	(563,467)
	\$ 699	\$ 13,854

Depreciation expense for the years ended December 31, 2014 and 2013 was approximately \$13,155 and \$33,000, respectively. Depreciation expense related to leasehold improvements and equipment in our warehouse is allocated to cost of goods sold. All other depreciation is included in general and administrative expense.

8. Accrued Liabilities

Accrued liabilities consist of the following:

	December 31, 2014	December 31, 2013
Accrued salaries, wages, benefits and bonus	\$ 45,586	\$ 45,456
Sales tax payable	662	4,409
Customer deposit payable	41,265	580
Accrued interest	5,683	6,288
Other accrued liabilities	11,033	32,997
	\$ 104,229	\$ 89,730

9. Convertible Notes Payable and Credit Facility

Convertible Notes payable

On August 30, 2013, we entered into a securities purchase agreement with Alpha Capital Anstalt ("Alpha Capital") relating to the sale and issuance of a convertible note in the principal amount of \$200,000 that matures August 29, 2015 (the "Convertible Note"). Subsequently, on November 25, 2013 and December 19, 2013, we entered into additional securities purchase agreements with Alpha Capital relating to the sale and issuance of convertible notes in the principal amount of \$200,000 and \$250,000, respectively, which mature on November 25, 2015 and December 19, 2015. On January 27, 2014, we issued a convertible note in the principal amount of \$100,000 that matures January 27, 2016 under the Securities Purchase Agreement we entered into with Alpha Capital on December 19, 2013. In connection with the issuance of the December 19, 2013 convertible note, we also issued 6,250,000 warrants to purchase shares of our common stock at a price of \$0.02 per share. On February 25, 2014, we entered into a Securities Purchase Agreement with the Alpha Capital related to the sale and issuance of a convertible note in the principal amount of \$200,000 that matures February 25, 2016. In connection with the issuance of the February 25, 2014 convertible note, we issued 5,000,000 warrants to purchase shares of our common stock at a price of \$0.02 per share. On March 18, 2014, we entered into a Securities Purchase Agreement we entered into with the Alpha Capital related to the sale and issuance of a convertible note in the principal amount of \$300,000 that matures March 18, 2016.

In connection with the March 18, 2014 convertible note, we issued a five-year warrant to purchase 7,500,000 shares of our common stock at an exercise price of \$0.02 per share. Each of the Convertible Notes bear interest at the rate of 8% per annum compounded annually, are payable at maturity and the principal and interest outstanding under the convertible notes are convertible into shares of our common stock, at any time after issuance, at the option of the purchaser, at a conversion price equal to \$0.02 per share, subject to adjustment upon the happening of certain events, including stock dividends, stock splits and the issuance of common stock equivalents at a price below the conversion price. Subject to our fulfilling certain conditions, including beneficial ownership limits, the convertible notes are subject to a mandatory conversion if the closing price of our common stock for any 20 consecutive days commencing six months after the issue date of the convertible notes equal or exceeds \$0.04. Unless waived in writing by the purchaser, no conversion of the convertible notes can be effected to the extent that as a result of such conversion the purchaser would beneficially own more than 9.99% in the aggregate of our issued and outstanding common stock immediately after giving effect to the issuance of common stock upon conversion.

As of December 31, 2014, convertible notes in the principal amount of \$940,000, along with accrued interest of \$68,319, were converted into 50,439,751 shares of our common stock.

We have the option of repaying the outstanding principal amount of the convertible notes, in whole or in part, by paying the purchaser a sum of money equal to one hundred and twenty percent (120%) of the principal together with accrued but unpaid interest upon 30 days' notice, subject to certain beneficial ownership limits. For so long as we have any obligation under the convertible notes, we have agreed to certain restrictions regarding, among other things, incurrence of additional debt, liens, amendments to charter documents, repurchase of stock, payment of cash dividends, affiliated transactions. We are also prohibited from entering into certain variable priced agreements until the convertible notes are repaid in full, except for the Equity Line we have with Southridge.

Because of certain down-round protection in the conversion rate of the convertible notes, we determined that the derivative liability related to embedded conversion feature met the criteria for bifurcation. Accordingly, we recognized an aggregate liability of \$123,000 on the three issuance dates during the year ended December 31, 2014. This was in addition to the carrying value of the derivative liability on three previously recorded derivatives of \$178,000. The derivative liability is carried at fair value with changes in the fair value reflected in the "Adjustment to the fair value of embedded derivatives" line item of our condensed consolidated statements of operations. We recognized a non-cash benefit for the year ended December 31, 2014 of \$51,000 on a total of six convertible notes.

In addition, the relative fair value of the warrants issued in the December 2013 convertible note issuance of \$250,000, were allocated to additional paid-in capital. Such value was determined assuming volatility of 149.1%, a risk free interest rate of 0.7% and an expected term of 4.1 years. The resulting debt discount from the derivative liability and warrant issuance of \$109,000 is being accreted to interest using the effective interest method. The relative fair value of the warrants issued in the February 2014 convertible note issuance of \$200,000, were allocated to additional paid-in capital. Such value was determined assuming volatility of 169.1, a risk free interest rate of 0.7% and an expected term of 4.1 years. The resulting debt discount from the derivative liability and warrant issuance of \$101,000 is being accreted to interest using the effective interest method. The relative fair value of the warrants issued in the March 2014 convertible note issuance of \$300,000, were allocated to additional paid-in capital. Such value was determined assuming volatility of 168.8%, a risk free interest rate of 0.8% and an expected term of 4.1 years. The resulting debt discount from the derivative liability and warrant issuance of \$154,000 is being accreted to interest using the effective interest method.

On November 1 and December 1, 2013, and on January 1, February 1 and March 1, 2014, we issued convertible notes to our financial advisory firm in the principal amount of \$30,000 each for a total of \$150,000, which mature on October 31, November 30 and December 31, 2014, and on January 31 and February 28, 2015, respectively. On April 1, May 1 and June 1, 2014, we issued convertible notes to our financial advisory firm in the principal amount of \$20,000 each, for a total of \$60,000, which mature on March 31, April 30 and May 31, 2015, respectively. On July 1, 2014, we issued convertible notes to our financial advisory firm in the principal amount of \$10,000, which matures on June 30, 2015. Each of the Convertible Notes bear interest at the rate of 8% per annum compounded annually, are payable at maturity and the principal and interest outstanding under the convertible notes are convertible into shares of our common stock, at any time after issuance, at the option of the purchaser, at a conversion price equal to \$0.02 per share. Unless waived in writing by the purchaser, no conversion of the convertible notes can be effected to the extent that as a result of such conversion the purchaser would beneficially own more than 9.99% in the aggregate of our issued and outstanding common stock immediately after giving effect to the issuance of common stock upon conversion.

Below is a table showing the convertible notes payable, the derivative liability and fair value of the warrants as of December 31, 2014 and 2013:

	December 31, 2014	December 31, 2013
Convertible notes payable	\$ 520,000	\$ 650,000

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Convertible notes payable issued for financial advisory services	10,000	60,000
Less: Derivative liability	(93,376)	(243,889)
Less: Relative fair value of warrants	(170,767)	(53,623)
Accreted interest	79,358	21,889
Accrued interest	28,284	7,707
Convertible notes payable, net	373,499	442,084
Less current portion	(30,000)	(60,000)
	\$ 343,499	\$ 382,084

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Line of credit

On September 30, 2013, we entered into a loan and security agreement with Alpha Capital Anstalt and Collateral Services, LLC to provide financing, on a discretionary basis, for one year, against our accounts receivable and inventory. The maximum amount that could be borrowed under the Agreement is \$500,000. We had the right to borrow up to 80% of our eligible accounts receivable, not in excess of \$200,000, 50% of the value of our raw materials in inventory, 65% of our finished goods inventory and 95% of cash, but not in the aggregate amount in excess of \$300,000. The advances were secured by a lien on all of our assets. All advances under the agreement bear interest at a per annum rate of 12% and monthly interest shall be a minimum of \$500. At the time of initial funding we paid a loan fee of 50 shares of our Series D Preferred Shares to the lender, in addition to other payments for legal fees. In addition, we paid the collateral agent an initial fee of \$5,000 and have agreed to pay an administrative fee to the collateral agent of 0.5% per month of the daily balance during the preceding month or \$500 whichever is less. In the event that of a prepayment, we are obligated to pay a prepayment fee in an amount equal to one-half of one percent (0.5%) of \$500,000. On September 30, 2013, we requested and received an initial borrowing under the Agreement totaling \$350,000. Subsequently, on October 21, 2013, we requested and received an additional \$100,000 and on November 20, 2013, we requested and received an additional \$50,000. As of December 31, 2014, the balance outstanding under our line of credit was \$500,000. On February 27, 2015, we agreed to extend the term of the agreement for one year, and to exchange the \$500,000 plus interest owing under the agreement for a one year, 8%, convertible note. We are no longer able to make borrowings under the agreement.

10. Long-term Debt

Long-term debt

Our long-term debt consists of three convertible notes amounting to an aggregate principal amount of \$500,000, and are scheduled to mature in 2016.

11. Stockholders' Equity

We have 501,000,000 shares of capital stock authorized under our certificate of incorporation, consisting of 500,000,000 shares of common stock and 1,000,000 shares of preferred stock. As of September 30, 2014, we have authorized (i) 2,000 shares of Series A Convertible Preferred Stock, par value \$0.001, (ii) 4,000 shares of Series B 4% Convertible Preferred Stock, par value \$0.001, (iii) 1,175 shares of our Series C 8% Convertible Preferred Stock, par value \$0.001, and (iv) 1,180 shares of our Series D 8% Convertible Preferred Stock, par value \$0.001. All preferred stock has been converted or cancelled and none remain outstanding

On March 11, 2014, we filed a Registration Statement on Form S-1/A to register 35 million shares of common stock related to our Prior Equity Purchase Agreement with Southridge and on March 21, 2014, the Securities and Exchange Commission declared the Registration Statement effective. On March 26, 2014, we submitted an initial take-down request of \$300,000 to Southridge pursuant to the terms of the Prior Equity Purchase Agreement and issued 12,541,806 shares of our common stock, of which partial proceeds of \$100,000 was received on March 31, 2014 and \$200,000 was received on April 16, 2014. On April 17, 2014, we issued 8,079,800 shares of our common stock in a Section 3(a) (10) proceeding that generated proceeds in the amount of \$250,000 in full settlement of a claim (see Note 17. Commitments and Contingencies). On June 4, 2014, June 18, 2014, July 8, 2014, and October 25, 2014, we submitted additional take-down requests for \$100,000, \$100,000, \$125,000, and approximately \$52,000 respectively, pursuant to the terms of the Prior Equity Purchase Agreement. We issued a total of 44,079,800 shares of our common stock at an average price of \$0.02 per share pursuant to the terms of the Prior Equity Purchase Agreement.

Pursuant to the terms of our Equity Purchase Agreement, a placement fee of 1 million shares of unregistered common stock was due to Southridge pursuant to the terms of the Equity Purchase Agreement. During March 2014, we issued 500,000 shares of unregistered common stock due upon the declaration of effectiveness of our Form S-1/A by the Securities and Exchange Commission of our Form S-1/A. In April 2014, we issued the remaining 500,000 shares of unregistered common stock to Southridge upon the completion of our initial take-down request under the Prior Equity Purchase Agreement.

On December 10, 2014, we entered into the December Equity Purchase Agreement with Southridge, that superseded our Prior Equity Purchase Agreement with Southridge that was entered into on January 23, 2014. The terms of the December Equity Purchase Agreement are substantially similar to those of the Prior Equity Purchase Agreement. Pursuant to the December Equity Purchase Agreement and as provided in the Prior Equity Purchase Agreement, Southridge has committed to purchase up to \$5,000,000 worth of our common stock, over a period of time terminating on the earlier of: (i) 18 months from the effective date of the registration statement to be filed by us for the Equity Purchase Agreement; or (ii) the date on which Southridge has purchased an aggregate maximum purchase price of \$5,000,000 pursuant to the December Equity Purchase Agreement; Southridge's commitment to purchase our common stock is subject to various conditions, including, but not limited to, limitations based on the trading volume of our common stock.

Pursuant to the terms of the December Equity Purchase Agreement we agreed to pay Southridge a commitment fee of 1,000,000 shares of our common stock (having a value of \$17,900 based upon the closing price of our common stock on December 5, 2014), of which 500,000 shares of our common stock were issued to Southridge on the date that the registration statement was declared effective, January 16, 2015, and the remaining 500,000 shares of common stock were issued on the date that we delivered our first Draw Down Notice to Southridge.

On December 10, 2014, we also entered into a Registration Rights Agreement with Southridge pursuant to which we agreed to register shares of the common stock to be issued to Southridge in connection with the December Equity Purchase Agreement.

See Note 14 for a discussion of the accounting treatment of the stock warrant transactions discussed above.

12. Convertible Redeemable Preferred Stock and Preferred Deemed Dividend

On January 24, 2013, we provided to the purchasers of our Series C Preferred Stock a draw down notice under the Purchase Agreement. The purchasers agreed to accept the new draw down notice and thereby extend our right to exercise a "put" to sell additional Series C Preferred beyond the securities purchase agreement's prior expiration date of December 31, 2012. As a result of the draw down, we sold an aggregate of 75 additional shares of Series C Preferred to the purchasers for aggregate proceeds of \$75,000. Based on the closing price of our common stock as reported on the OTCQB Marketplace on January 24, 2013 (which was \$0.05 per share), the 75 shares of Series C Preferred to be issued pursuant to the draw down would be convertible into 1,500,000 shares of our common stock. As a result of the contingent conversion feature on the Series C Preferred, which reduced the conversion price from \$0.08 to \$0.05 per share on the total 720 shares of Series C Preferred Stock issued and outstanding at January 24, 2013, and which resulted in an increase in the number of common shares issuable, we recognized additional preferred deemed dividends of \$270,000.

As a result of the January 24, 2013 draw down notice, the conversion price of the Series C Preferred issued under the initial closing was reduced from \$0.08 per share of common stock to become equal to \$0.05. As a result of the May 13, 2013 draw down notice, the conversion price of the Series C Preferred was further reduced from \$0.05 per share of common stock to \$0.03 per share. As a result of our August 30, 2013 financing, the conversion price of the Series C

Preferred was further reduced from \$0.03 per share of common stock to \$0.02 per share.

On February 15, 2013, we entered into a securities purchase agreement with an institutional accredited investor relating to the sale and issuance of up to 1,180 shares of our newly created Series D Preferred Stock at a price per share equal to the stated value, which is \$1,000 per share, for aggregate proceeds of up to \$1,000,000. At the initial closing, concurrent with entering the agreement, we issued 150 shares of Series D Preferred, for initial aggregate proceeds of \$150,000. After the initial closing, the securities purchase agreement permits the purchaser to exercise a "call" right to purchase additional Series D Preferred in multiple draw downs from time to time until December 31, 2013, subject to certain limits, terms and conditions. In March 2013, the Company and investors entered into a letter agreement to the securities purchase agreement dated as of February 15, 2013, modifying the number of shares of Series D Preferred Stock to be issued upon settlement of any purchaser draw downs made on or after March 18, 2013, equal to the purchaser investment amount divided by the stated value multiplied by a number agreed upon by the Company and the purchaser, which shall not be higher than \$1.67. Subsequently, on March 21, 2013, we issued 167 shares of Series D Preferred for aggregate proceeds of \$100,000. On May 13, 2013, the Company and investors entered into a letter agreement amendment to the securities purchase agreement dated as of February 15, 2013, modifying the number of shares of Series D Preferred Stock that may be issued upon draw downs made on or after May 13, 2013, equal to the purchaser investment amount divided by the stated value multiplied by a number agreed upon by the Company and the purchaser, which shall not be higher than \$3.34. The corresponding conversion price into underlying shares of our common stock was \$0.03 per share. On May 13, 2013, we issued 583 shares of Series D Preferred to an investor for aggregate proceeds of \$175,000. As a result of the contingent conversion feature on the Series C Preferred, which reduced the conversion price from \$0.05 to \$0.03 per share on the total 260 shares of Series C Preferred Stock issued and outstanding as of May 13, 2013, and which resulted in an increase in the number of common shares issuable, we recognized additional preferred deemed dividends of \$104,000. On August 30, 2013, we entered into an agreement to sell \$200,000 in convertible notes. As a result of the sale of these convertible notes and as a result of the contingent conversion feature on the Series C Preferred and Series D Preferred, which reduced the conversion price from \$0.03 to \$0.02 per share on the Series C and from \$0.10 to \$0.02 per share on the Series D on the total 147 shares and 930 shares, respectively, of Series C Preferred Stock and Series D Preferred Stock issued and outstanding as of August 30, 2013, and which resulted in an increase in the number of common shares issuable, we recognized additional preferred deemed dividends of \$36,000 on the Series C Preferred Stock and \$465,000 on the Series D Preferred Stock. The net loss attributable to common shareholders reflects both the net loss and the deemed dividend. As a result of the \$500,000 loan and security agreement entered into on September 30, 2013, we issued to the lender 50 shares of our Series D Preferred stock for the \$50,000 loan origination fee.

During the year ended December 31, 2014, the remaining 467 shares of Series B Preferred Stock were converted into 21,020,015 shares of common stock, the remaining 87 shares of Series C Preferred Stock were converted into 4,333,350 shares of common stock and the remaining 860 shares of Series D Preferred Stock were converted into 43,000,000 shares of common stock.

See Note 12 for a discussion of the accounting treatment of the stock warrant transactions described above.

13. Stock Option and Incentive Plan

On August 8, 2006, we adopted the Andalay Solar, Inc. 2006 Stock Incentive Plan (the “Stock Plan”) pursuant to which shares of common stock are available for issuance to employees, directors and consultants under the Stock Plan as restricted stock and/or options to purchase common stock. At our Annual Meeting of Stockholders held on September 19, 2013, our stockholders approved and adopted an amendment to our 2006 Incentive Stock Plan, increasing the number of shares of our common stock reserved for issuance under the Plan from 3,000,000 to 50,000,000.

Restricted stock and options to purchase common stock may be issued under the Stock Plan. The restriction period on restricted stock grants generally expire at a rate of 25% per quarter over one year or 25% per year over four years, unless decided otherwise by our Compensation Committee. Options to purchase common stock generally vest and become exercisable at a rate of 25% per quarter over one year or as to one-third of the total amount of shares subject to the option on each of the first, second and third anniversaries from the date of grant. Options to purchase common stock generally have a 5-year term.

We use the Black-Scholes-Merton Option Pricing Model (Black-Scholes) to estimate fair value of our employee and our non-employee director stock-based awards. Black-Scholes requires various judgmental assumptions, including estimating stock price volatility, expected option life and forfeiture rates. If we had made different assumptions, the amount of our deferred stock-based compensation, stock-based compensation expense, gross margin, net loss and net loss per share amounts could have been significantly different. We believe that we have used reasonable methodologies, approaches and assumptions to determine the fair value of our common stock, and that our deferred stock-based compensation and related amortization were recorded properly for accounting purposes. If any of the assumptions we used change significantly, stock-based compensation expense may differ materially in the future from that recorded in the current period.

We measure compensation expense for non-employee stock-based compensation under ASC 505-50, “Equity-Based Payments to Non-Employees.” The fair value of the option issued is used to measure the transaction, as this is more reliable than the fair value of the services received. The estimated fair value is measured utilizing Black-Scholes using the value of our common stock on the date that the commitment for performance by the counterparty has been reached or the counterparty’s performance is complete (generally the vesting date). The fair value of the equity instrument is charged directly to expense and additional paid-in capital.

We recognized stock-based compensation expense of approximately \$224,000 and \$110,000 during the years ended December 31, 2014 and 2013, respectively, relating to compensation expense calculated based on the fair value at the time of grant for restricted stock and based on Black-Scholes for stock options granted under the Stock Plan.

The following table sets forth a summary of restricted stock activity for the years ended December 31, 2014 and 2013:

	Number of Restricted Shares	Weighted-Average Grant Date Fair Value
Outstanding and not vested beginning balance as of January 1, 2013	48,073	\$ 2.50
Granted	2,500,000	\$ 0.03
Forfeited/cancelled	(21,798)	\$ 2.46
Released/vested	(635,323)	\$ 0.08
Outstanding and not vested beginning balance as of January 1, 2014	1,890,952	\$ 0.05
Granted	—	\$ —
Forfeited/cancelled	—	\$ —
Released/vested	(1,883,766)	\$ 0.04

Outstanding and not vested as of December 31, 2014	7,186	\$	2.16
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Restricted stock is valued at the grant date fair value of the common stock and expensed over the requisite service period or vesting period. We estimate forfeitures when recognizing stock-based compensation expense for restricted stock, and the estimate of forfeitures is adjusted over the requisite service period should actual forfeitures differ from such estimates. As of December 31, 2014, there was approximately \$1,000 of unrecognized stock-based compensation expense associated with the granted but unvested restricted stock. Stock-based compensation expense relating to these restricted shares is being recognized over a weighted-average period of 0.2 years. The total fair value of shares vested during the years ended December 31, 2014 and 2013, was approximately \$64,000 and \$19,000, respectively. Tax benefits resulting from tax deductions in excess of the compensation cost recognized (excess tax benefits) are classified as financing cash flows on our consolidated statements of cash flows. During the years ended December 31, 2014 and 2013, there were no excess tax benefits relating to restricted stock and therefore there is no impact on the accompanying consolidated statements of cash flows.

The following table sets forth a summary of stock option activity for the years ended December 31, 2014 and 2013:

	Number of Shares Subject To Option 2014		Number of Shares Subject To Option 2013	
		Weighted-Average Exercise Price		Weighted-Average Exercise Price
Outstanding beginning balance	6,618,233	\$ 0.11	679,744	\$ 2.82
Granted during the year	30,456,250	0.02	6,400,000	0.03
Forfeited/cancelled/expired during the year	(40,000)	5.15	(461,511)	3.29
Exercised during the year	—	—	—	—
Outstanding at end of year	37,034,483	\$ 0.03	6,618,233	\$ 0.11
Exercisable at end of year	5,934,303	\$ 0.09	2,330,650	\$ 0.28
Outstanding and expected to vest	36,916,502	\$ 0.03	6,191,212	\$ 0.11

Stock options are valued at the estimated fair value on the grant date or the measurement date and expensed over the requisite service period or vesting period. The weighted-average volatility was based upon the historical volatility of our common stock price. The fair value of stock option grants during the years ended December 31, 2014 and 2013 was estimated using the Black-Scholes option-pricing model with the following assumptions:

	Years Ended December 31,	
	2014	2013
Weighted-average volatility	185.0%	105.5%
Expected dividends	0.0%	0.0%
Expected life	3.5 years	2.0 years
Weighted-average risk-free interest rate	1.1%	0.30%

The weighted-average fair value per share of the stock options as determined on the date of grant was \$0.02 for the stock options to purchase 30,456,250 shares of common stock granted during the years ended December 31, 2014 and \$0.02 for the stock options to purchase 6,400,000 share of common stock granted during the years ended December 31, 2013. The weighted-average remaining contractual term for the stock options outstanding (vested and expected to vest) and exercisable as of December 31, 2014 and 2013, was 4.4 and 4.7 years, respectively. The total estimated fair value of stock options vested during the years ended December 31, 2014 and 2013 was approximately \$91,000 and \$81,000, respectively. The aggregate intrinsic value of stock options outstanding as of December 31, 2014 and 2013 was zero.

We estimate forfeitures when recognizing stock-based compensation expense for stock options and the estimate of forfeitures is adjusted over the requisite service period should actual forfeitures differ from such estimates. As of December 31, 2014 there was approximately \$514,000 of unrecognized stock-based compensation expense associated with stock options granted. Stock-based compensation expense relating to these stock options is being recognized over a weighted-average period of 0.7 years and 1.0, respectively. Tax benefits resulting from tax deductions in excess of the compensation cost recognized (excess tax benefits) is classified as financing cash flows on our consolidated statements of cash flows. During the years ended December 31, 2014 and 2013, there were no excess tax benefits relating to stock options and therefore there is no impact on the accompanying consolidated statements of cash flows.

Non-vested stock option activity for the year ended December 31, 2014 is as follows:

	Non-Vested Stock Options	Weighted-Average Grant Date Fair Value
Outstanding as of January 1, 2014	4,287,583	\$ 0.02
Granted	30,456,250	\$ 0.02
Forfeited/cancelled	(40,000)	\$ 3.04
Released/vested	(3,637,403)	\$ 0.02
Outstanding as of December 31, 2014	31,066,430	\$ 0.02

Options outstanding as of December 31, 2014 are summarized as follows:

	Options Outstanding			Vested Options		
	Number Outstanding	Weighted- Average Remaining Contractual Life (in years)	Weighted- Average Exercise Price	Number Outstanding	Weighted- Average Exercise Price	
\$0.0192	12,450,000	4.6	\$ 0.02	358,320	\$ 0.02	
\$0.020 - \$0.023	18,000,000	4.6	\$ 0.02	1,125,000	\$ 0.02	
\$0.0296	6,400,000	3.8	\$ 0.0296	4,266,500	\$ 0.0296	
\$0.11 - \$5.32	184,483	1.3	\$ 1.95	184,483	\$ 1.95	
\$0.0192 - \$5.32	37,034,483	4.4	\$ 0.03	5,934,303	\$ 0.09	

14. Stock Warrants and Warrant Liability

During March 2009, in connection with an equity financing, we issued Series E Warrants to purchase 334,822 shares of common stock at an exercise price of \$5.36 per share. The fair value of the warrants was estimated using Black-Scholes with the following weighted average assumptions: risk-free interest rate of 2.69%, an expected life of five years; an expected volatility factor of 112% and a dividend yield of 0.0%. The value assigned to these warrants was approximately \$1.0 million, of which \$1.0 million was reflected as common stock warrant liability with an offset to additional paid-in capital as of the offering close date. The fair value of the warrants decreased to zero as of December 31, 2013.

On December 19, 2013 and February 25, 2014, we entered into securities purchase agreements with Alpha Capital Anstalt relating to the sale and issuance of a (i) convertible notes in the principal amount of \$250,000, \$200,000 and \$300,000 that mature on December 19, 2015, February 25, 2016 and March 19, 2016, respectively and (ii) five- year warrants (with a cashless exercise feature under certain circumstances) to purchase 6,250,000, 5,000,000 and 7,500,000 shares, respectively, of our common stock at an exercise price of \$0.02 per share, subject to adjustment under certain circumstances. See Note 9 for further discussion of the issuance of the convertible note.

The following table summarizes the Warrant activity for the year ended December 31, 2014:

	Warrants for Number of Shares	Weighted-Average Exercise Price
Outstanding as of December 31, 2013	9,648,045	\$ 0.49
Issued	12,500,000	0.02
Exercised	—	—
Cancelled/expired	—	—
Outstanding as of December, 2014	22,148,045	\$ 0.23

The majority of our warrants outstanding are not exercisable for nine months from the date of issuance and are exercisable for either 4.5 years or 5 years thereafter. Our outstanding warrants expire on various dates between December 2015 and March 2019.

15. Fair Value Measurement

We use a fair-value approach to value certain assets and liabilities. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or liability. We use a fair value hierarchy, which distinguishes between assumptions based on market data (observable inputs) and an entity's own assumptions (unobservable inputs). The hierarchy consists of three levels:

- Level one — Quoted market prices in active markets for identical assets or liabilities;
- Level two — Inputs other than level one inputs that are either directly or indirectly observable; and
- Level three — Unobservable inputs developed using estimates and assumptions, which are developed by the reporting entity and reflect those assumptions that a market participant would use.

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Determining which category an asset or liability falls within the hierarchy requires significant judgment. We evaluate our hierarchy disclosures each quarter. Assets and liabilities measured at fair value on a recurring basis are summarized as follows:

Liabilities	Level 1	Level 2	Level 3	December 31, 2014
Fair value of embedded derivatives		—	—\$ 129,598	\$ 129,598
Total	\$	—\$	—\$ 129,598	\$ 129,598

Liabilities	Level 1	Level 2	Level 3	December 31, 2013
Fair value of embedded derivatives	\$	—\$	—\$ 177,927	\$ 177,927
Total	\$	—\$	—\$ 177,927	\$ 177,927

On August 30, 2013, November 25, 2013 and December 19, 2013, we entered into securities purchase agreements relating to the sale and issuance of convertible notes in the principal amounts of \$200,000, \$200,000 and \$250,000. Each of the Convertible Notes are convertible into shares of our common stock, at any time after issuance, at the option of the purchaser, at a conversion price equal to \$0.02, subject to adjustment upon the happening of certain events, including stock dividends, stock splits and the issuance of common stock equivalents at a price below the conversion price. Subject to our fulfilling certain conditions, including beneficial ownership limits, the convertible notes are subject to a mandatory conversion if the closing price of our common stock for any 20 consecutive days commencing six months after the issue date of the convertible notes equal or exceeds \$0.04 per share. The terms of the convertible notes meet the criteria for the bifurcation of an embedded derivative. Therefore, we recorded the fair value of the embedded derivative liability as of the issuance date for each of the convertible notes for an aggregate fair value of \$243,889.

We use a model based on Monte Carlo simulation to value the embedded conversion feature of our notes payable that are subject to fair value liability accounting. The determination of the fair value as of the reporting date is affected by our stock price as well as assumptions regarding a number of highly complex and subjective variables. These variables include, but are not limited to, expected stock price volatility over the term of the security and risk-free interest rate. In addition, the model uses multiple Monte Carlo simulations requiring the input of an expected life for the securities for which we have estimated and expectations of the timing and amount of future financing we may require. The fair value of the embedded conversion feature liability is revalued each balance sheet date utilizing our Monte Carlo simulation-based model computations with the decrease or increase in fair value being reported in the statement of comprehensive loss as other income or expense, respectively. The primary factors affecting the fair value of the embedded conversion feature liability are our stock price and volatility. In addition, the use of a Monte Carlo simulation-based model requires the input of highly subjective assumptions, and other reasonable assumptions could provide differing results.

Our reported net loss was approximately \$1.9 million for the year ended December 31, 2014. If the closing stock price of our common stock had been 10% lower, our net loss would have been approximately \$15,000 lower. If the closing stock price of our common stock had been 10% higher, our net loss would have been approximately \$26,000 higher. If our volatility assumption on December 31, 2014 had been 10% lower, our net loss would have been approximately \$7,000 lower and if our volatility assumption had been 10% higher, our net loss would have been approximately \$13,000 higher.

The following table shows the changes in Level 3 liabilities measured at fair value on a recurring basis for the years ended December 31, 2014:

Explanation of Responses:

	Embedded Derivative on Convertible Notes	Total Level 3
Beginning balance – January 1, 2014	\$ 177,927	\$ 177,927
Issuances	122,630	122,630
Total realized and unrealized gains or losses	(50,809)	(50,809)
Transfers out of level 3 upon exercise or conversion	(221,768)	(221,768)
Ending balance – December 31, 2014	\$ 129,598	\$ 129,598

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16. Income Taxes

During the years ended December 31, 2014, and 2013, respectively, there was no income tax expense or benefit for federal and state income taxes in the accompanying consolidated statements of operations due to our net loss and a valuation allowance on the resulting deferred tax assets.

The actual tax expense differs from the “expected” tax expense for the years ended December 31, 2014 and 2013 (computed by applying the U.S. Federal Corporate tax rate of 34% to income before taxes) as follows:

	December 31, 2014	December 31, 2013
Tax at federal statutory rate	\$ (740,000)	\$ (967,000)
State taxes, net of federal benefit	(117,000)	(160,000)
Research and development credits	—	(12,000)
Fair market value of warrants & derivatives	17,000	(22,000)
Stock-based compensation	51,000	29,000
Other permanent items	10,000	1,000
Valuation allowance	779,000	1,131,000
Income tax provision	\$ —	\$ —

The tax effects of temporary differences that give rise to significant portions of deferred tax assets and liabilities as of December 31, 2014 and 2013 are as follows:

	December 31, 2014	December 31, 2013
Deferred tax assets:		
Net operating loss and credit carryforwards	\$ 30,227,000	\$ 29,431,000
Stock-based compensation	1,199,000	1,193,000
Stock-based compensation	422,000	558,000
Basis difference for fixed assets and intangibles	158,000	174,000
Total gross deferred tax assets	32,006,000	31,356,000
Valuation allowance	(32,006,000)	(31,356,000)
Net deferred tax assets	\$ —	\$ —

A valuation allowance is provided when it is more likely than not that some portion of the deferred tax assets will not be realized. We established a 100% valuation allowance due to the uncertainty of realizing future tax benefits from its net operating loss carryforwards and other deferred tax assets. At December 31, 2014, we had useable net operating loss carryforwards of approximately \$75.2 million for federal and \$73.1 million for state income tax purposes available to offset future taxable income expiring through 2033 for both federal and California. At December 31, 2014, we had useable R & D credits of approximately \$361,000 for federal and \$231,000 for California. The federal credits expire through 2032 and the state credits have no expiration. The net change in the valuation allowance during the years ended December 31, 2014 and 2013 was an increase of approximately \$650,000 and \$1.1 million, respectively, primarily due to current year losses.

Internal Revenue Code Section 382 places a limitation (the "Section 382 Limitation") on the amount of taxable income, which can be offset by net operating loss carryforwards after a change in control (generally greater than a 50% change in ownership) of a loss corporation. Generally, after a control change, a loss corporation cannot deduct operating loss carryforwards in excess of the Section 382 Limitation. Due to these "change in ownership" provisions, utilization of the net operating loss and tax credit carryforwards may be subject to an annual limitation regarding their utilization against taxable income in future periods. The company has not concluded its analysis of Section 382 through December 31, 2014 but believes that these provisions will not limit the availability of losses to offset future income.

On January 1, 2007, the Company adopted ASC Topic 740—Income Taxes ("ASC 740") FASB ASC 740, Income Taxes—an interpretation of FASB Statement No. 109 ("FIN 48"). Due to net operating loss and research credit carryforwards, substantially all of the Company's tax years remain open to U.S. federal and state tax examinations. The Company classifies interest and penalties recognized pursuant to Interpretation 48 as part of income tax expense. No interest or penalties related to unrecognized tax benefits have been accrued for the year ended December 31, 2014.

The aggregate changes in the balance of gross unrecognized tax benefits were as follows (in thousands):

	2014	2013
Balance, beginning of year	\$ 147,000	\$ 140,000
Additions based on tax positions related to the current year	—	—
Additions for tax positions related to prior years	—	7,000
Reductions for tax positions related to prior years	—	—
Balance, end of year	\$ 147,000	\$ 147,000

In the event that any unrecognized tax benefits are recognized, the effective tax rate will be affected. Approximately \$128,000 and \$128,000 as of December 31, 2014 and 2013 respectively, of unrecognized tax benefits would impact the effective rate, if recognized.

17. Commitments and Contingencies

Westinghouse License

On May 17, 2010, we entered into an exclusive worldwide agreement that permits us to manufacture, distribute and market our solar panels under the Westinghouse name. On August 23, 2013, the license agreement with Westinghouse, Inc. was terminated.

Operating Leases

Our principal executive offices and warehouse premises are located at 2071 Ringwood Ave., Unit C, San Jose, CA 95128. On or around May 1, 2015, our corporate headquarters is relocating to 48900 Milmont Drive, Fremont, CA 94538. Commencing March 1, 2014, the monthly rent for our warehouse has been \$10,500. The monthly rent during 2013 and in January and February 2014 was \$7,800. We consolidated our executive offices with our warehouse premises effective January 1, 2014. Our warehouse lease agreement expired on February 28, 2015 and we are on a month-to-month rental agreement.

Litigation

We are also involved in other litigation from time to time in the ordinary course of business. In the opinion of management, the outcome of such proceedings will not materially affect our financial position, results of operations or cash flows.

18. Concentration of Risk in Customer and Supplier Relationships

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Supplier Relationships

In September 2013, we entered into a supply agreement for assembly of our proprietary modules with Tianwei New Energy Co, Ltd. (“Tianwei”), a panel supplier located in China. We began receiving product from Tianwei in February 2014 and stopped as of June 2014. In July 2014, we entered into a supply agreement for assembly of our proprietary modules with Auxin Solar, Inc., a panel supplier located in the United States. We began receiving product from Auxin in December 2014. Although we believe we can find alternative suppliers for solar panels manufactured to our specifications, our operations would be disrupted unless we are able to rapidly secure alternative sources of supply, our inventory and revenue could diminish significantly, causing disruption to our operations.

Historically, we obtained virtually all of our solar panels from Suntech and Lightway. During 2012, because of our cash position and liquidity constraints, we were late in making payments to both of these suppliers. On March 30, 2012, pursuant to our Supply Agreement with Lightway, we issued 1,900,000 shares of our common stock to Lightway in partial payment of our past due account payable to them. At the time of issuance, the shares were valued at \$1,045,000. On May 1, 2012, Suntech filed a complaint for breach of contract, goods sold and delivered, account stated and open account against us in the Superior Court of the State of California, County of San Francisco. Suntech alleged that it delivered products and did not receive full payment from us. On July 31, 2012, we and Suntech entered into a settlement of this dispute. Because of our inability to make scheduled settlement payments, on March 15, 2013, Suntech entered a judgment against us in the amount of \$946,438. As of December 31, 2014, Suntech has not sought to enforce its judgment. As of December 31, 2014, we have included in accounts payable in our consolidated balance sheets a balance due to Suntech America of \$946,438. We currently have no unshipped orders from Suntech or Lightway.

Customer Relationships

The relative magnitude and the mix of revenue from our largest customers have varied significantly quarter to quarter. During the year ended December 31, 2014, five customers have accounted for significant revenues, varying by period, to our company: Smart Energy Today (“Smart Energy”), which specializes in helping home owners and business owners become more energy efficient, WDC Solar, Inc. (“WDC”), a leading construction, integration and installation of commercial, residential and utility scale solar installations in the Washington D.C. area, JCF Wholesale (“JCF”) a provider of residential and commercial electrical services in Southern California, Lowe’s Companies, Inc. (Lowe’s), a nationwide home improvement retail chain, and Sustainable Environmental Enterprises (“SEE”), a leading provider of renewable energy and development projects located in New Orleans, Louisiana. For the year ended December 31, 2014 and 2013, the percentages of sales of our top five customers are as follows:

	Years Ended December 31,	
	2014	2013
Smart Energy Today	13.3%	13.5%
WDC Solar, Inc.	12.0%	14.7%
JCF Wholesale	8.7%	10.6%
Lowe’s	5.9%	6.9%
Sustainable Environmental Enterprises	1.3%	52.8%

The percentage of our gross accounts receivable for our top customers as of December 31, 2014 and 2013, are as follows:

	December 31,	
	2014	2013
WDC Solar, Inc.	40.1%	—
Lowe's	16.8%	—
Sustainable Environmental Enterprises	—	86.7%
Smart Energy Today	6.5%	—

We maintain reserves for potential credit losses and such losses, in the aggregate, have generally not exceeded management's estimates. Our top three vendors accounted for approximately 39% and 25% of purchases as of December 31, 2014 and 2013, respectively. As of December 31, 2014 and 2013, accounts payable included amounts owed to these top three suppliers of approximately \$0 and \$1.0 million, respectively.

19. Employee Benefit Plan

On December 14, 2007, the Board of Directors approved the 401(k) profit sharing plan (the "401(k) Plan") effective January 1, 2008. Employees began deferring a portion of their compensation into the 401(k) Plan commencing on January 1, 2008. In 2011, we began making matching contributions equal to 10% of the employee contribution. For the years ended December 31, 2014 and 2013, there was no accrual relating to this matching contribution.

20. Subsequent Events

On February 9, 2015, the law firm of Snell & Wilmer LLP filed suit against us in California Superior Court, County of Orange. The complaint alleges that we have failed to pay Snell & Wilmer fees due to that firm in connection with prior patent prosecution litigation, in an amount of no less than \$808,202, plus interest. We are still evaluating the merits of the claim. As of December 31, 2014, we have included in accounts payable in our Consolidated Balance Sheets a balance due to Snell & Wilmer of \$808,202.

On December 10, 2014, we entered into an Equity Purchase Agreement (the "December Equity Purchase Agreement") with Southridge Partners II, LP ("Southridge"), that superseded our prior Equity Purchase Agreement with Southridge that was entered into on January 23, 2014 (the "Prior Equity Purchase Agreement"). The terms of the December Equity Purchase Agreement are substantially similar to those of the Prior Equity Purchase Agreement.

Pursuant to the December Equity Purchase Agreement and as provided in the Prior Equity Purchase Agreement, Southridge has committed to purchase up to \$5,000,000 worth of our common stock, over a period of time terminating on the earlier of: (i) 18 months from the effective date of the registration statement to be filed by us for the December Equity Purchase Agreement; or (ii) the date on which Southridge has purchased an aggregate maximum purchase price of \$5,000,000 pursuant to the December Equity Purchase Agreement; Southridge's commitment to purchase our common stock is subject to various conditions, including, but not limited to, limitations based on the trading volume of our common stock.

We submitted various take-down requests during the first quarter of 2015 pursuant to the terms of the December Equity Purchase Agreement. As of April 10, 2015, 53,781,201 shares had been sold at an average price of \$0.013 per share, resulting in total proceeds of approximately \$780,000.

Andalay Solar, Inc.
Condensed Consolidated Balance Sheets

	March 31, 2015 (unaudited)	December 31, 2014 (1)
Assets		
Current assets:		
Cash	\$ 135,377	\$ 61,542
Accounts receivable, net	62,386	118,456
Inventory	701,945	728,372
Prepaid expenses and other current assets	315,377	280,066
Total current assets	1,215,085	1,188,436
Property and equipment, net	350	699
Patents, net	1,144,342	1,131,327
Other assets, net	199,005	240,478
Total assets	\$ 2,558,782	\$ 2,560,940
Liabilities and Stockholders' Deficit		
Current liabilities:		
Accounts payable	\$ 3,220,948	\$ 3,345,361
Accrued liabilities	204,793	104,229
Accrued warranty	934,088	938,466
Deferred revenue	—	15,450
Derivative liability – embedded conversion feature	—	129,598
Line of credit	—	500,000
Note payable – short-term	73,129	109,164
Convertible note and beneficial conversion feature – short-term	247,985	30,000
Total current liabilities	4,680,943	5,172,268
Convertible notes, less current portion (net of discount)	—	343,499
Total liabilities	4,680,943	5,515,767
Commitments and contingencies (Note 17)		
Stockholders' deficit:		
Common stock, \$0.001 par value; 500,000,000 shares authorized; 372,254,399 and 279,475,332 shares issued and outstanding as of March 31, 2015 and December 31, 2014, respectively	372,254	279,475
Additional paid-in capital	83,592,015	82,026,952
Accumulated deficit	(86,086,430)	(85,261,254)
Total stockholders' deficit	(2,122,161)	(2,954,827)
Total liabilities and stockholders' deficit	\$ 2,558,782	\$ 2,560,940

(1) The condensed consolidated balance sheet as of December 31, 2014 has been derived from the audited consolidated financial statements as of that date.

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

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Andalay Solar, Inc.
Condensed Consolidated Statements of Comprehensive Loss
(Unaudited)

	Three Months Ended March 31,	
	2015	2014
Net revenue	\$ 274,641	\$ 142,482
Cost of goods sold	286,382	135,388
Gross profit (loss)	(11,741)	7,094
Operating expenses		
Sales and marketing	71,129	63,384
General and administrative	721,358	604,164
Total operating expenses	792,487	667,548
Loss from continuing operations	(804,228)	(660,454)
Other income (expense)		
Interest income (expense), net	(62,213)	(77,085)
Adjustment to the fair value of embedded derivatives	41,265	(101,551)
Settlement of prior debt owed	—	769,148
Total other income (expense), net	(20,948)	590,512
Loss before provision for income taxes	(825,176)	(69,942)
Provision for income taxes	—	—
Net loss	(825,176)	(69,942)
Preferred stock dividend	—	(14,454)
Net loss attributable to common stockholders	\$ (825,176)	\$ (84,396)
Net loss attributable to common stockholders per common share (basic and diluted)	\$ (0.00)	\$ (0.00)
Weighted-average shares used in computing loss per common share:	327,997,747	131,428,001

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

Andalay Solar, Inc.

Condensed Consolidated Statements of Changes in Stockholders' Deficit
(Unaudited)

	Common Stock		Additional	Accumulated	Stockholders'
	Number of	Amount	Paid-in	Deficit	Deficit
	Shares		Capital		
Balance as of January 1, 2015	279,475,332	\$ 279,475	\$ 82,026,952	\$ (85,261,254)	\$ (2,954,827)
Issuance of common stock pursuant to equity purchase agreement	58,213,490	58,214	777,634	—	835,848
Beneficial conversion feature on issuance of convertible note	—	—	275,000	—	275,000
Issuance of common stock upon conversion of note payable	34,565,577	34,565	443,829	—	478,394
Stock-based compensation	—	—	68,600	—	68,600
Net loss	—	—	—	(825,176)	(825,176)
Balance as of March 31, 2015	372,254,399	\$ 372,254	\$ 83,592,015	\$ (86,086,430)	\$ (2,122,161)

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

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Andalay Solar, Inc.
Condensed Consolidated Statements of Cash Flows
(Unaudited)

	Three Months Ended	
	March 31,	
	2015	2014
Cash flows from operating activities		
Net loss	\$ (825,176)	\$ (69,942)
Adjustments to reconcile net loss to net cash used in operations:		
Depreciation	349	4,920
Amortization	29,358	28,347
Bad debt expense	(2,909)	4,492
Unrealized (gain) loss on fair value of embedded derivatives	(41,265)	101,551
Accretion of interest on convertible note	6,345	25,964
Accretion of interest on debt discount	22,985	—
Non-cash stock-based compensation expense	68,600	75,822
Non-cash settlement of prior debt owed	—	(769,148)
Accrued interest payable	13,730	15,987
Changes in assets and liabilities:		
Accounts receivable	68,036	34,263
Other receivables	—	(178,624)
Inventory	26,427	(153,547)
Prepaid expenses and other current assets	19,966	86,391
Other assets	41,473	6,755
Accounts payable	(124,413)	96,524
Accrued liabilities and accrued warranty	84,079	(18,317)
Deferred revenue	(15,450)	—
Net cash used in operating activities	(627,865)	(708,562)
Cash flows from investing activities		
Acquisition of patents	(42,373)	—
Net cash used in investing activities	(42,373)	—
Cash flows from financing activities		
Borrowing on convertible notes payable	—	600,000
Repayment notes payable	(36,035)	(42,929)
Proceeds from issuance of common stock	780,108	—
Borrowing on line of credit	—	300,000
Repayments on capital lease obligations	—	(299)
Payment of placement agent and registration fees and other direct costs	—	(36,616)
Employee taxes paid for vesting of restricted stock	—	(2,714)
Net cash provided by financing activities	744,073	817,442
Net increase in cash	73,835	108,880
Cash		
Beginning of period	61,542	150,081
End of period	\$ 135,377	\$ 258,961
Supplemental cash flows disclosures:		
Cash paid during the period for interest	\$ 939	\$ 20,254
Supplemental disclosure of non-cash financing activity:	\$ —	\$ —

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Embedded derivative on convertible note issued	\$ 176,771	\$ 122,630
Embedded derivative converted to equity	\$ 88,333	\$ 221,768
Receivable for issuance of common stock	\$ 55,277	\$ —
Grant of warrants on issue of convertible note	\$ —	\$ 170,767
Refinance of line of credit to convertible note payable	\$ 500,000	\$ —
Preferred stock dividend	\$ —	\$ 14,454
Common stock issued for equity purchase agreement fees	\$ 12,107	\$ —
Conversion of preferred stock to common stock	\$ —	\$ 465,053
Conversion of convertible note to common stock	\$ 570,531	\$ —
Beneficial conversion feature on note refinance	\$ 275,000	\$ —
Convertible note issued to financial advisor in exchange for service	\$ —	\$ 90,000

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

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Andalay Solar, Inc.
Notes to Condensed Consolidated Financial Statements
March 31, 2015
(Unaudited)

1. Basis of Presentation and Description of Business

Basis of Presentation — Interim Financial Information

The accompanying condensed consolidated financial statements are unaudited and have been prepared in accordance with generally accepted accounting principles for interim financial information. They should be read in conjunction with the consolidated financial statements and related notes to the consolidated financial statements of Andalay Solar, Inc. (“we”, “us”, “our” or the “Company”), formerly Westinghouse Solar, Inc. and Akeena Solar, Inc., for the years ended December 31, 2014 and 2013 appearing in our Form 10-K. The March 31, 2015 unaudited interim condensed consolidated financial statements included in this Quarterly Report on Form 10-Q have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission (“SEC”). Certain information and note disclosures normally included in annual financial statements filed with our Annual Report on Form 10-K have been condensed or omitted as permitted by those rules and regulations. In the opinion of management, all adjustments, consisting of normal recurring accruals, necessary for a fair statement of the results of operations for the interim periods presented have been reflected herein. The results of operations for interim periods are not necessarily indicative of the results to be expected for the entire year.

Description of Business

Andalay Solar, Inc. and its subsidiaries (Andalay Solar, the Company, we, us or our) is a designer and manufacturer of integrated solar power systems and solar panels with integrated microinverters (which we call AC solar panels). We design, market and sell these solar power systems to solar installers and do-it-yourself customers in the United States, Canada, the Caribbean and South America through distribution partnerships, our dealer network and retail outlets. Our products are designed for use in solar power systems for residential and commercial rooftop customers. Prior to September 2010, we were also in the solar power installation business, but decided to exit that business. During the fourth quarter 2014, we re-entered the solar power installation business. Additionally, we are engaging in a new strategy of licensing our patented products to large module manufacturers and entering into distribution agreements with these manufacturers and large national distributors/installers. This new strategy is less capital intensive and aligns us with companies that have proven track records in the residential solar industry.

We were incorporated in February 2001 as Akeena Solar, Inc. in the State of California and elected at that time to be taxed as an S corporation. During June 2006, we reincorporated in the State of Delaware and became a C corporation. On August 11, 2006, we entered into a reverse merger transaction with Fairview Energy Corporation, Inc. (“Fairview”). Pursuant to the merger, our stockholders received one share of Fairview common stock for each issued and outstanding share of our common stock. Our common shares were also adjusted from \$0.01 par value to \$0.001 par value at the time of the Merger. On May 17, 2010, we entered into an exclusive worldwide license agreement with Westinghouse, Inc, which permitted us to manufacture, distribute and market solar panels under the Westinghouse name and in connection therewith, on April 6, 2011, we changed our name to Westinghouse Solar, Inc. On April 13, 2011, we effected a reverse split of our common stock at a ratio of 1 – for – 4. On August 23, 2013, the license agreement with Westinghouse, Inc. was terminated and on September 19, 2013, we changed our name to our current name, Andalay Solar, Inc. and increased our number of authorized shares of common stock to 500,000,000.

Our Corporate headquarters is located at 48900 Milmont Drive, Fremont, CA 94538. Our telephone number is (408) 402-9400. Additional information about Andalay Solar is available on our website at <http://www.andalaysolar.com>.

The information on our web site is not incorporated herein by reference.

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2. Significant Accounting Policies

Liquidity and Financial Position

We currently face challenges meeting the working capital needs of our business. Our primary requirements for working capital are to fund purchases for solar panels and microinverters, and to cover our payroll and lease expenses. We have incurred net losses and negative cash flows from operations for the three months ended March 31, 2015 and for each of the years ended December 31, 2014 and 2013. During recent years, we have undertaken several equity and debt financing transactions to provide the capital needed to sustain our business. We have dramatically reduced our headcount and other variable expenses. As of March 31, 2015, we had approximately \$135,000 in cash on hand. We intend to address ongoing working capital needs through sales of remaining inventory, along with raising additional debt and equity financing. Our revenue levels remain difficult to predict, and as we anticipate we will continue to sustain losses in the near term, we cannot assure investors that we will be successful in reaching break-even.

In September 2013, we entered into a supply agreement for assembly of our proprietary modules with Tianwei New Energy Co, Ltd., a panel supplier located in China. We began receiving product from Tianwei in February 2014 and stopped as of June 2014. In July 2014, we entered into a supply agreement for assembly of our proprietary modules with Auxin Solar, Inc., a panel supplier located in the United States. In December 2014, we began distributing panels from our new supplier. Although we believe we can find alternative suppliers for solar panels manufactured to our specifications, our operations would be disrupted unless we are able to rapidly secure alternative sources of supply, our inventory and revenue could diminish significantly, causing disruption to our operations.

The accompanying consolidated financial statements have been prepared assuming we will continue as a going concern. Our significant operating losses, negative cash flow from operations, and challenges in rapidly securing alternative sources of supply for solar panels, raise substantial uncertainty about our ability to continue as a going concern. The accompanying financial statements do not include any adjustments that might result from the outcome of this uncertainty, and contemplate the realization of assets and the settlement of liabilities and commitments in the normal course of business. There can be no assurance that we will be able to raise additional funds on commercially reasonable terms, if at all. There is uncertainty to our anticipated revenue levels and to the timing of cash receipts, which are needed to support our operations. It also worsens the market conditions for seeking equity and debt financing. We currently anticipate that we will retain all of our earnings, if any, for development of our business and do not anticipate paying any cash dividends on common stock in the foreseeable future.

Securities Purchase Agreement

Because of certain down-round protection in the conversion rate of the convertible notes, we determined that the derivative liability related to the embedded conversion feature met the criteria for bifurcation. Accordingly, we recognized an aggregate liability of \$123,000 on the three issuance dates during the year ended December 31, 2014. This was in addition to the carrying value of the derivative liability on three previously recorded derivatives of \$178,000. The derivative liability is carried at fair value with changes in the fair value reflected in the "Adjustment to the fair value of embedded derivatives" line item of our condensed consolidated statements of operations. We recognized a non-cash benefit for the three months ended March 31, 2015 of approximately \$41,000 on a total of three convertible notes.

In addition, the relative fair value of the warrants issued in the December 2013 convertible note issuance of \$250,000, were allocated to additional paid-in capital. Such value was determined assuming volatility of 149.1%, a risk free interest rate of 0.7% and an expected term of 4.1 years. The resulting debt discount from the derivative liability and warrant issuance of \$109,000 is being accreted to interest using the effective interest method. The relative fair value of the warrants issued in the February 2014 convertible note issuance of \$200,000, were allocated to additional paid-in

capital. Such value was determined assuming volatility of 169.1, a risk free interest rate of 0.7% and an expected term of 4.1 years. The resulting debt discount from the derivative liability and warrant issuance of \$101,000 is being accreted to interest using the effective interest method. The relative fair value of the warrants issued in the March 2014 convertible note issuance of \$300,000, were allocated to additional paid-in capital. Such value was determined assuming volatility of 168.8%, a risk free interest rate of 0.8% and an expected term of 4.1 years. The resulting debt discount from the derivative liability and warrant issuance of \$154,000 is being accreted to interest using the effective interest method.

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On November 1 and December 1, 2013, and on January 1, February 1 and March 1, 2014, we issued convertible notes to our financial advisory firm in the principal amount of \$30,000 each for a total of \$150,000, which mature on October 31, November 30 and December 31, 2014, and on January 31 and February 28, 2015, respectively. On April 1, May 1 and June 1, 2014, we issued convertible notes to our financial advisory firm in the principal amount of \$20,000 each, for a total of \$60,000, which mature on March 31, April 30 and May 31, 2015, respectively. On July 1, 2014, we issued convertible notes to our financial advisory firm in the principal amount of \$10,000, which matures on June 30, 2015. Each of the Convertible Notes bear interest at the rate of 8% per annum compounded annually, are payable at maturity and the principal and interest outstanding under the convertible notes are convertible into shares of our common stock, at any time after issuance, at the option of the purchaser, at a conversion price equal to \$0.02 per share. Unless waived in writing by the purchaser, no conversion of the convertible notes can be effected to the extent that as a result of such conversion the purchaser would beneficially own more than 9.99% in the aggregate of our issued and outstanding common stock immediately after giving effect to the issuance of common stock upon conversion.

Equity Purchase Agreement

On January 23, 2014, we entered into an Equity Purchase Agreement with Southridge Partners II, LP (“Southridge”), that superseded our prior Equity Purchase Agreement with Southridge that was entered into on November 25, 2013 (the “Prior Equity Purchase Agreement”). The terms of the new Equity Purchase Agreement are identical to those of the Prior Equity Purchase Agreement other than that the New Equity Purchase Agreement provides that the Agreement may not be amended by either party. Pursuant to the New Equity Purchase Agreement and as provided in the Prior Equity Purchase Agreement, Southridge has committed to purchase up to \$5,000,000 worth of our common stock, over a period of time terminating on the earlier of: (i) 18 months from the effective date of the registration statement to be filed by us for the New Equity Purchase Agreement; or (ii) the date on which Southridge has purchased an aggregate maximum purchase price of \$5,000,000 pursuant to the New Equity Purchase Agreement; Southridge’s commitment to purchase our common stock is subject to various conditions, including, but not limited to, limitations based on the trading volume of our common stock. On March 11, 2014, we filed a Registration Statement on Form S-1/A to register 35 million shares of common stock related to our Equity Purchase Agreement with Southridge and on March 21, 2014, the Securities and Exchange Commission declared the Registration Statement effective. On March 26, 2014, we submitted an initial take-down request of \$300,000 to Southridge pursuant to the terms of the Equity Purchase Agreement of which partial proceeds of \$100,000 was received on March 31, 2014 and \$200,000 on April 16, 2014. On June 4, 2014, June 18, 2014 and July 8, 2014, we submitted additional take-down requests for \$100,000, \$100,000 and \$125,000, respectively, pursuant to the terms of the Equity Purchase Agreement.

On December 10, 2014, we entered into the December Equity Purchase Agreement with Southridge, that superseded our Prior Equity Purchase Agreement with Southridge that was entered into on January 23, 2014. The terms of the December Equity Purchase Agreement are substantially similar to those of the Prior Equity Purchase Agreement. Pursuant to the December Equity Purchase Agreement and as provided in the Prior Equity Purchase Agreement, Southridge has committed to purchase up to \$5,000,000 worth of our common stock, over a period of time terminating on the earlier of: (i) 18 months from the effective date of the registration statement to be filed by us for the Equity Purchase Agreement; or (ii) the date on which Southridge has purchased an aggregate maximum purchase price of \$5,000,000 pursuant to the December Equity Purchase Agreement; Southridge’s commitment to purchase our common stock is subject to various conditions, including, but not limited to, limitations based on the trading volume of our common stock. We submitted various take-down requests during the first quarter of 2015 pursuant to the terms of the December Equity Purchase Agreement. As of May 12, 2015, 67,813,489 shares had been sold at an average price of \$0.0137 per share, resulting in total proceeds of approximately \$929,000.

Pursuant to the terms of the December Equity Purchase Agreement we agreed to pay Southridge a commitment fee of 1,000,000 shares of our common stock, of which 500,000 shares of our common stock were due to Southridge on

January 16, 2015, the date that the registration statement was declared effective and the remaining 500,000 shares of common stock were due on January 20, 2015, the date that we delivered our first Draw Down Notice to Southridge. We valued the issuance of these shares based on the closing price of the stock as of January 16, 2015, \$0.0169 for 500,000, and as of January 20, 2015, \$0.0161 for 500,000, and we recorded \$16,500 as a reduction in "Additional Paid In Capital" on our condensed consolidated balance sheets.

On December 10, 2014, we also entered into a Registration Rights Agreement with Southridge pursuant to which we agreed to register shares of the common stock to be issued to Southridge in connection with the December Equity Purchase Agreement.

Settlement of Potential Claims Agreement

On January 22, 2014, we entered into a Settlement of Potential Claims Agreement with ASC Recap LLC ("ASCR"). Pursuant to the Agreement, ASCR has offered to purchase (and in one (1) case has already purchased) approximately \$3.7 million of our prior debt owed to four creditors ("Creditors") for past due services at a substantial discount to face value to which we have agreed to issue to ASCR certain shares of our common stock in a §3(a)(10) 1933 Act proceeding. The shares of our common stock that we have agreed to issue to ASCR in full payment for, and as a release of any debt it purchases from the Creditors, is anticipated to have, upon issuance, a market value equal to approximately 25% of the principal amount of our outstanding debt. In the case of the debt ASCR already purchased from one (1) Creditor, we entered into a Settlement Agreement and Stipulation on February 26, 2014 that was filed with the Circuit Court of the Second Judicial Circuit, Leon County, Florida pursuant to which we agreed, subject to court approval, to issue shares of our common stock that generate proceeds in the amount of \$250,000 in full settlement of the claim in the amount of \$1,027,705 that ASCR acquired from one Creditor (the value of the stock that we have agreed to issue was two hundred and fifty percent (250%) of the discounted purchase price ASCR paid to purchase the debt from the Creditor, and approximately 25% of the original amount we owed to the Creditor), resulting in a gain on settlement of \$769,148, net of expenses. On March 24, 2014, the Circuit Court of the Second Judicial Circuit, Leon County, Florida, approved the §3(a)(10) 1933 Act proceeding and Settlement Agreement and Stipulation and in April 2014, we issued 8,079,800 shares of common stock at an average price of \$0.031 for the full settlement of the agreement with ASCR.

Use of Estimates

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

Revenue Recognition

Revenue from sales of products is recognized when: (1) persuasive evidence of an arrangement exists, (2) delivery has occurred or services have been rendered, (3) the sale price is fixed or determinable, and (4) collection of the related receivable is reasonably assured. We recognize revenue when the solar power systems are shipped to the customer. Revenue from installation of a system is recognized when (1) persuasive evidence of an arrangement exists, (2) delivery has occurred or services have been rendered, (3) the sales price is fixed or determinable, and (4) collection of the related receivable is reasonably assured. In general, we recognize revenue upon completion of a system installation for residential installations and we recognize revenue under the percentage-of-completion method for commercial installations. Revenue recognition methods for revenue streams that fall under other categories are determined based on facts and circumstances.

Cash and Cash Equivalents

We consider all highly liquid investments with maturities of three months or less, when purchased, to be cash equivalents. We maintain cash and cash equivalents which consist principally of demand deposits with high credit quality financial institutions. At certain times, such amounts exceed FDIC insurance limits. We have not experienced any losses on these investments and, as of March 31, 2015 and December 31, 2014, we had no cash equivalents.

Accounts Receivable

Accounts receivable consist of trade receivables. We regularly evaluate the collectibility of our accounts receivable. An allowance for doubtful accounts is maintained for estimated credit losses, and such losses have historically been minimal and within our expectations. We consider a number of factors when estimating credit losses, including the aging of a customer's account, creditworthiness of specific customers, historical trends and other information.

Manufacturer and Installation Warranties

The manufacturer directly warrants the solar panels and inverters for a range from 15 to 25 years. We warrant the balance of system components of our products against defects in material and workmanship for five years. We assist our customers in the event of a claim under the manufacturer warranty to replace a defective solar panel or inverter. The warranty liability for the material and the workmanship of the balance of system components of approximately \$366,000 as of March 31, 2015 and \$345,000 at December 31, 2014, is included within "Accrued warranty" in the accompanying consolidated balance sheets.

The liability for our manufacturing warranty consists of the following:

	March 31, 2015	December 31, 2014
Beginning accrued warranty balance	\$ 938,466	\$ 1,312,918
Reduction for labor payments and claims made under the warranty	(13,998)	(75,966)
Adjustment to warranty liability for discontinued operations		— (324,349)
Accruals related to warranties issued during the period	9,620	25,863

Explanation of Responses:

Ending accrued warranty balance	\$ 934,088	\$ 938,466
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Patent Costs

We capitalize external legal costs and filing fees associated with obtaining or defending our patents. Upon issuance of new patents or successful defense of existing patents, we amortize these costs using the straight line method over the shorter of the legal life of the patent or its economic life. We believe the remaining useful life we assign to these patents, approximately 9.75 years as of March 31, 2015, are reasonable. We periodically review our patents to determine whether any such cost have been impaired and are no longer being used. To the extent we are no longer using certain patents, the associated costs will be written off at that time.

Significant Accounting Policies and Estimates

There have been no material developments or changes to the significant accounting policies discussed in our 2014 Annual Report on Form 10-K or accounting pronouncements issued or adopted, except as described below.

Segment Reporting

We are engaged in two business segments, (i) we sell our AC solar panels to solar installers, trade workers and do-it-yourself customers through distribution partnerships, our dealer network and retail outlets and (ii) we market, sell, design and install systems for residential and commercial customers. Operating segments are components of an enterprise for which separate financial information is available and is evaluated regularly by management in deciding how to allocate resources and in assessing performance. During the fourth quarter 2014, we re-entered the solar power installation business. See Note 3 for financial information on our business segments.

Recent Accounting Pronouncements

In April 2015, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") ASU 2015-03 Interests — Imputation of Interest (Subtopic 835-30), Simplifying the Presentation of Debt Issuance Costs , requires that debt issuance costs be presented in the balance sheet as a direct deduction from the carrying amount of the debt liability. Recognition and measurement guidance are not impacted by the ASU. The guidance is effective for fiscal years beginning after December 15, 2015, with retrospective disclosure upon transition, for all periods presented. We do not expect there to be any impact on the consolidated financial statements as a result of this guidance.

In February 2015, the FASB issued ASU 2015-02 Consolidation (Topic 810) Amendments to the Consolidation Analysis . Effective for fiscal years beginning after December 15, 2015, the update effects the consolidation criteria around limited partnerships and similar legal entities; evaluation of fees paid to a decision maker or a service provider as a variable interest; the determination of primary beneficiary of a variable interest entity (VIE) when fee arrangements exist, the treatment of related parties in the VIE consolidation model and the consolidation of certain investment funds. We do not expect there to be any impact on the consolidated financial statements as a result of this guidance.

In January 2015, ASU 2015-01 Income Statement — Extraordinary and Unusual Items (Subtopic 225-20) Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items , was issued by the FASB. The ASU eliminates the concept of extraordinary items. Presentation and disclosure guidance for items that are unusual in nature or occur infrequently will be expanded to include items that are both unusual in nature and infrequent in occurrence. The guidance is effective for years beginning after December 15, 2015 and will be adopted in the first quarter of 2016. We do not expect there to be any impact on the consolidated financial statements as a result of this guidance.

In August 2014, the FASB issued ASU No. 2014-15, "Presentation of Financial Statements – Going Concern: Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern" ("ASU 2014-15"), to provide guidance on management's responsibility in evaluating whether there is substantial doubt about a company's ability to continue as a going concern and to provide related footnote disclosures. ASU 2014-15 is effective for the annual period ending after December 15, 2016, and for annual periods and interim periods thereafter. Since ASU 2014-15 only impacts financial statement disclosure requirements regarding whether there is substantial doubt about an entity's ability to continue as a going concern, we do not expect its adoption to have an impact on our consolidated financial statements.

In November 2014, the FASB issued ASU No. 2014-16, Determining Whether the Host Contract in a Hybrid Financial Instrument Issued in the Form of a Share Is More Akin to Debt or to Equity. The amendments in this ASU do not change the current criteria in U.S. GAAP for determining when separation of certain embedded derivative features in a hybrid financial instrument is required. The amendments clarify that an entity should consider all relevant terms and features, including the embedded derivative feature being evaluated for bifurcation, in evaluating the nature of the host contract. The ASU applies to all entities that are issuers of, or investors in, hybrid financial instruments that are issued in the form of a share and is effective for public business entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. Early adoption is permitted. We do not expect there to be any impact on the consolidated financial statements as a result of this guidance.

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Reclassifications

Certain prior year amounts have been reclassified for consistency with the current period presentation. These reclassifications had no effect on the reported results of operations.

3. Segment Reporting

We are engaged in two business segments, (i) we market, sell, design and install systems for residential and commercial customers and (ii) we sell our AC solar panels to solar installers, trade workers and do-it-yourself customers through distribution partnerships, our dealer network and retail outlets. Operating segments are components of an enterprise for which separate financial information is available and is evaluated regularly by management in deciding how to allocate resources and in assessing performance.

An analysis of our revenue, operating profit and total assets are as follows (unaudited):

	Three Months Ended March 31,	
	2015	2014
Revenue		
Distribution	\$ 166,136	\$ 142,482
Installation	108,505	—
	\$ 274,641	\$ 142,482

	Three Months Ended March 31,	
	2015	2014
Gross profit (loss)		
Distribution	\$ (9,975)	\$ 7,094
Installation	(1,766)	—
	\$ (11,741)	\$ 7,094

	March 31,	December
	2015	31, 2014
Assets		
Distribution	\$ 2,482,508	\$ 2,560,940
Installation	20,997	—
	\$ 2,503,505	\$ 2,560,940

We do not allocate operating expenses or other income (expense) to any of these segments for internal reporting purposes, as we do not believe that allocating these expenses is beneficial in evaluating segment performance. Installation assets include only accounts receivable assets. Other than accounts receivable, we do not allocate assets to segments for internal reporting purposes as we do not manage our segments by such metrics.

4. Other Assets

We entered into a Supply and Warranty Agreement and Master Assignment Agreement with Real Goods Solar, Inc. (“Real Goods”), pursuant to which Real Goods has agreed to perform certain warranty work. The terms of the agreement provide that an escrow account be established as a source of funds from which to satisfy our obligation to pay Real Goods for its fees and reimburse it for its expenses for this warranty work. In March 2011, we entered into an Escrow Agreement with Real Goods and deposited \$200,000 into an escrow account. In accordance to the Escrow Agreement, the escrow deposit will be released to us in the amount of \$40,000, or one-fifth of the remaining escrow funds, per year after each of the fifth through the ninth anniversary of the escrow agreement, although we believe that the amount may be redeemed earlier. In December 2014, \$110,000 of the funds in escrow were returned by Real Goods. As of March 31, 2015, there was \$90,000 remaining in escrow, which is included under “Other assets, net” in our condensed consolidated balance sheets.

5. Accounts Receivable

Accounts receivable consists of the following:

	March 31, 2015	December 31, 2014
Trade accounts	\$ 104,005	\$ 154,172
Less: Allowance for bad debts	(21,972)	(24,882)
Less: Allowance for returns	(19,647)	(10,834)
	\$ 62,386	\$ 118,456

The following table summarizes the allowance for doubtful accounts as of March 31, 2015 and December 31, 2014:

	Balance as of Beginning of Period	Provisions, net	Write-Off/ Recovery	Balance as of End of Period
Three months ended March 31, 2015	\$ 24,882	\$ 2,909	\$ (5,819)	\$ 21,972
Year ended December 31, 2014	\$ 2,899	\$ 36,763	\$ (14,780)	\$ 24,882

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6. Inventory

Inventory consists of the following:

	March 31, 2015	December 31, 2014
Finished goods	\$ 631,616	\$ 669,706
Work in process	70,329	58,666
	\$ 701,945	\$ 728,372

Inventory is stated at the lower of cost (on an average basis) or market value. We determine cost based on our weighted-average purchase price and include both the costs of acquisition and the shipping costs in our inventory. We regularly review the cost of inventory against its estimated market value and record a lower of cost or market write-down to cost of goods sold, if any inventory has a cost in excess of estimated market value. We did not record a write-down of inventory during the three months ended March 31, 2015.

7. Property and Equipment, Net

Property and equipment, net consist of the following:

	March 31, 2015	December 31, 2014
Office equipment	\$ 436,051	\$ 436,051
Leasehold improvements	123,278	123,278
Vehicles	17,992	17,992
	577,321	577,321
Less: Accumulated depreciation and amortization	(576,971)	(576,622)
	\$ 350	\$ 699

Depreciation expense for the three months ended March 31, 2015 and 2014 was \$349 and \$4,920, respectively.

8. Accrued Liabilities

Accrued liabilities consist of the following:

	March 31, 2015	December 31, 2014
Accrued salaries, wages, benefits and bonus	\$ 63,876	\$ 45,586
Sales tax payable	3,646	662
Accrued accounting and legal fees	61,050	—
Customer deposit payable	33,604	41,265
Accrued interest	22,256	5,683
Other accrued liabilities	20,361	11,033
	\$ 204,793	\$ 104,229

9. Convertible Notes Payable and Credit Facility

Convertible Notes Payable

On August 30, 2013, we entered into a securities purchase agreement with Alpha Capital Anstalt (“Alpha Capital”) relating to the sale and issuance of a convertible note in the principal amount of \$200,000 that matures August 29, 2015 (the "Convertible Note"). Subsequently, on November 25, 2013 and December 19, 2013, we entered into additional securities purchase agreements with Alpha Capital relating to the sale and issuance of convertible notes in the principal amount of \$200,000 and \$250,000, respectively, which mature on November 25, 2015 and December 19, 2015. On January 27, 2014, we issued a convertible note in the principal amount of \$100,000 that matures on January 27, 2016 under the Securities Purchase Agreement we entered into with Alpha Capital on December 19, 2013. In connection with the issuance of the December 19, 2013 convertible note, we also issued 6,250,000 warrants to purchase shares of our common stock at a price of \$0.02 per share. On February 25, 2014, we entered into a securities purchase agreement with a certain institutional accredited investor relating to the sale and issuance of a (i) convertible note in the principal amount of \$200,000 that matures February 25, 2016 and (ii) five-year warrant (with a cashless exercise feature under certain circumstances) to purchase 5,000,000 shares of our common stock at an exercise price of \$0.02 per share, subject to adjustment under certain circumstances. On March 18, 2014, we issued under the Securities Purchase Agreement we entered into with the institutional investor on February 25, 2014 a (i) convertible note in the principal amount of \$300,000 that matures March 18, 2016 and (ii) five-year warrant (with a cashless exercise feature under certain circumstances) to purchase 7,500,000 shares of our common stock at an exercise price of \$0.02 per share, subject to adjustment under certain circumstances. The convertible notes bear interest at the rate of 8% per annum compounded annually, are payable at maturity and the principal and interest outstanding under the convertible notes are convertible into shares of our common stock, at any time after issuance, at the option of the purchaser, at a conversion price equal to \$0.02 per share, subject to adjustment upon the happening of certain events, including stock dividends, stock splits and the issuance of common stock equivalents at a price below the conversion price. During the three months ended March 31, 2015, the remaining outstanding convertible notes in the principal amount of approximately \$520,000, along with accrued interest of \$47,134, net of unamortized discount at date of conversion, were converted into 34,565,577 shares of our common stock.

Because of certain down-round protection in the conversion rate of the convertible notes, we determined that the derivative liability related to the embedded conversion feature met the criteria for bifurcation. Accordingly, we recognized an aggregate liability of \$123,000 on the three issuance dates during the year ended December 31, 2014. This was in addition to the carrying value of the derivative liability on three previously recorded derivatives of \$178,000. The derivative liability is carried at fair value with changes in the fair value reflected in the “Adjustment to

the fair value of embedded derivatives” line item of our condensed consolidated statements of operations. We recognized a non-cash benefit for the three months ended March 31, 2015 of approximately \$41,000 on a total of three convertible notes.

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In addition, the relative fair value of the warrants issued in the December 2013 convertible note issuance of \$250,000, were allocated to additional paid-in capital. Such value was determined assuming volatility of 149.1%, a risk free interest rate of 0.7% and an expected term of 4.1 years. The resulting debt discount from the derivative liability and warrant issuance of \$109,000 is being accreted to interest using the effective interest method. The relative fair value of the warrants issued in the February 2014 convertible note issuance of \$200,000, were allocated to additional paid-in capital. Such value was determined assuming volatility of 169.1, a risk free interest rate of 0.7% and an expected term of 4.1 years. The resulting debt discount from the derivative liability and warrant issuance of \$101,000 is being accreted to interest using the effective interest method. The relative fair value of the warrants issued in the March 2014 convertible note issuance of \$300,000, were allocated to additional paid-in capital. Such value was determined assuming volatility of 168.8%, a risk free interest rate of 0.8% and an expected term of 4.1 years. The resulting debt discount from the derivative liability and warrant issuance of \$154,000 is being accreted to interest using the effective interest method.

On November 1 and December 1, 2013, and on January 1, February 1 and March 1, 2014, we issued convertible notes to our financial advisory firm in the principal amount of \$30,000 each for a total of \$150,000, which mature on October 31, November 30 and December 31, 2014, and on January 31 and February 28, 2015, respectively. On April 1, May 1 and June 1, 2014, we issued convertible notes to our financial advisory firm in the principal amount of \$20,000 each, for a total of \$60,000, which mature on March 31, April 30 and May 31, 2015, respectively. On July 1, 2014, we issued convertible notes to our financial advisory firm in the principal amount of \$10,000, which matures on June 30, 2015. Each of the Convertible Notes bear interest at the rate of 8% per annum compounded annually, are payable at maturity and the principal and interest outstanding under the convertible notes are convertible into shares of our common stock, at any time after issuance, at the option of the purchaser, at a conversion price equal to \$0.02 per share. Unless waived in writing by the purchaser, no conversion of the convertible notes can be effected to the extent that as a result of such conversion the purchaser would beneficially own more than 9.99% in the aggregate of our issued and outstanding common stock immediately after giving effect to the issuance of common stock upon conversion.

Line of Credit

On September 30, 2013, we entered into a loan and security agreement (the "Loan Agreement") with Alpha Capital Anstalt ("Alpha Capital") and Collateral Services, LLC to provide financing, on a discretionary basis, for one year, against our accounts receivable and inventory. The maximum amount that could be borrowed under the Loan Agreement was \$500,000. We had the right to borrow up to 80% of our eligible accounts receivable, not in excess of \$200,000, 50% of the value of our raw materials in inventory, 65% of our finished goods inventory and 95% of cash, but not in the aggregate amount in excess of \$300,000. The advances were secured by a lien on all of our assets. All advances under the Loan Agreement bear interest at a per annum rate of 12% and monthly interest shall be a minimum of \$500. At the time of initial funding we paid a loan fee of 50 shares of our Series D Preferred Shares to the lender, in addition to other payments for legal fees. In addition, we paid the collateral agent an initial fee of \$5,000 and have agreed to pay an administrative fee to the collateral agent of 0.5% per month of the daily balance during the preceding month or \$500 whichever is less. In the event that of a prepayment, we are obligated to pay a prepayment fee in an amount equal to one-half of one percent (0.5%) of \$500,000. On September 30, 2013, we requested and received an initial borrowing under the Loan Agreement totaling \$350,000. Subsequently, on October 21, 2013, we requested and received an additional \$100,000 and on November 20, 2013, we requested and received an additional \$50,000. As of December 31, 2014, the balance outstanding under our line of credit was \$500,000. On February 27, 2015, we agreed to extend the term of the Loan Agreement for one year, and to exchange the \$500,000 plus interest owing under the Loan Agreement for a one year, 8%, convertible note. As of March 31, 2015, a \$500,000 convertible note, along with \$10,000 in accrued interest, was outstanding. We are no longer able to make borrowings under the Loan Agreement.

The convertible note is convertible at \$0.01 per share of common stock. On the date we issued the convertible note to Alpha Capital, our stock price was \$0.0155 per share of common stock. As a result of the difference between the stock price at the time of issuance and the conversion price, we recorded a beneficial conversion feature in the amount of \$275,000 as a reduction to the Convertible Note and an increase in additional paid in capital on our condensed consolidated balance sheets. The beneficial conversion feature is being amortized over the 12 month term of the Note. We recorded additional interest expense of approximately \$23,000 during the quarter ended March 31, 2015 related to the beneficial conversion feature.

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10. Stockholders' Deficit

We have 501,000,000 shares of capital stock authorized under our certificate of incorporation, consisting of 500,000,000 shares of common stock and 1,000,000 shares of preferred stock. As of September 30, 2014, we have authorized (i) 2,000 shares of Series A Convertible Preferred Stock, par value \$0.001, (ii) 4,000 shares of Series B 4% Convertible Preferred Stock, par value \$0.001, (iii) 1,175 shares of our Series C 8% Convertible Preferred Stock, par value \$0.001, and (iv) 1,180 shares of our Series D 8% Convertible Preferred Stock, par value \$0.001. All preferred stock has been converted or cancelled and none remain outstanding.

On March 11, 2014, we filed a Registration Statement on Form S-1/A to register 35 million shares of common stock related to our Equity Purchase Agreement with Southridge and on March 21, 2014, the Securities and Exchange Commission declared the Registration Statement effective. On March 26, 2014, we submitted an initial take-down request of \$300,000 to Southridge pursuant to the terms of the Equity Purchase Agreement of which partial proceeds of \$100,000 was received on March 31, 2014 and \$200,000 on April 16, 2014. On April 17, 2014, we issued 8,079,800 shares of our common stock in a Section 3(a) (10) proceeding that generated proceeds in the amount of \$250,000 in full settlement of a claim (see Note 17. Commitments and Contingencies). On June 4, 2014, June 18, 2014 and July 8, 2014, we submitted additional take-down requests for \$100,000, \$100,000 and \$125,000, respectively, pursuant to the terms of the Equity Purchase Agreement. We issued a total of 31,760,578 shares of our common stock at an average price of \$0.02 per share pursuant to the terms of the Equity Purchase Agreement. We have approximately 3.2 million shares remaining under our effective Form S-1 and available pursuant to the terms of our Equity Purchase Agreement following our take-downs through August 11, 2014.

Pursuant to the terms of our Equity Purchase Agreement, a placement fee of one million shares of unregistered common stock was due to Southridge pursuant to the terms of the Equity Purchase Agreement. As of March 31, 2014, we issued 500,000 shares of unregistered common stock due upon the declaration of effectiveness of our Form S-1/A by the Securities and Exchange Commission of our Form S-1/A. In April 2014, we issued the remaining 500,000 shares of unregistered common stock to Southridge upon the completion of our initial take-down request under the Equity Purchase Agreement. The sales of the above securities were deemed to be exempt from registration under the Securities Act in reliance upon Section 4(a) (2) of the Securities Act as transactions by an issuer not involving any public offering. The recipients of the securities in each of these transactions represented their intentions to acquire the securities for investment only and not with a view to or for sale in connection with any distribution thereof, and appropriate legends were placed upon the stock certificates issued in these transactions.

On December 10, 2014, we entered into the December Equity Purchase Agreement with Southridge, that superseded our Prior Equity Purchase Agreement with Southridge that was entered into on January 23, 2014. The terms of the December Equity Purchase Agreement are substantially similar to those of the Prior Equity Purchase Agreement. Pursuant to the December Equity Purchase Agreement and as provided in the Prior Equity Purchase Agreement, Southridge has committed to purchase up to \$5,000,000 worth of our common stock, over a period of time terminating on the earlier of: (i) 18 months from the effective date of the registration statement to be filed by us for the Equity Purchase Agreement; or (ii) the date on which Southridge has purchased an aggregate maximum purchase price of \$5,000,000 pursuant to the December Equity Purchase Agreement; Southridge's commitment to purchase our common stock is subject to various conditions, including, but not limited to, limitations based on the trading volume of our common stock. We submitted various take-down requests during the first quarter of 2015 pursuant to the terms of the December Equity Purchase Agreement. As of May 12, 2015, 67,813,489 shares had been sold at an average price of \$0.0137 per share, resulting in total proceeds of approximately \$929,000.

Pursuant to the terms of the December Equity Purchase Agreement we agreed to pay Southridge a commitment fee of 1,000,000 shares of our common stock, of which 500,000 shares of our common stock were due to Southridge on January 16, 2015, the date that the registration statement was declared effective and the remaining 500,000 shares of common stock were due on January 20, 2015, the date that we delivered our first Draw Down Notice to Southridge.

We valued the issuance of these shares based on the closing price of the stock as of January 16, 2015, \$0.0169 for 500,000, and as of January 20, 2015, \$0.0161 for 500,000, and we recorded \$16,500 as a reduction in “Additional Paid In Capital” on our condensed consolidated balance sheets.

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11. Stock Option Plan and Stock Incentive Plan

On August 8, 2006, we adopted the Akeena Solar, Inc. 2006 Stock Incentive Plan (the “Stock Plan”) pursuant to which shares of common stock are available for issuance to employees, directors and consultants under the Stock Plan as restricted stock and/or options to purchase common stock. The Stock Plan allows for issuance of up to 50,000,000 shares and there were 45,593,221 shares available for issuance under the Stock Plan as of March 31, 2015.

Restricted stock and options to purchase common stock may be issued under the Stock Plan. The restriction period on restricted stock grants generally expires at a rate of 25% per year over four years, unless decided otherwise by our Compensation Committee. Options to purchase common stock generally vest and become exercisable as to one-third of the total amount of shares subject to the option on each of the first, second and third anniversaries from the date of grant. Options to purchase common stock generally have a 5-year term.

We use the Black-Scholes-Merton Options Pricing Model (“Black-Scholes”) to estimate fair value of our employee and our non-employee director stock-based awards. Black-Scholes requires various judgmental assumptions, including estimating stock price volatility, expected option life and forfeiture rates. If we had made different assumptions, the amount of our deferred stock-based compensation, stock-based compensation expense, gross margin, net loss and net loss per share amounts could have been significantly different. We believe that we have used reasonable methodologies, approaches and assumptions to determine the fair value of our common stock, and that our deferred stock-based compensation and related amortization were recorded properly for accounting purposes. If any of the assumptions we used change significantly, stock-based compensation expense may differ materially in the future from that recorded in the current period.

We measure compensation expense for non-employee stock-based compensation under ASC 505-50, “Equity-Based Payments to Non-Employees.” The fair value of the option issued is used to measure the transaction, as this is more reliable than the fair value of the services received. The estimated fair value is measured utilizing Black-Scholes using the value of our common stock on the date that the commitment for performance by the counterparty has been reached or the counterparty’s performance is complete (generally the vesting date). The fair value of the equity instrument is charged directly to expense and additional paid-in capital.

We recognized stock-based compensation expense of approximately \$68,600 and \$166,000 during the three months ended March 31, 2015 and 2014, respectively, relating to compensation expense calculated based on the fair value at the time of grant for restricted stock and based on Black-Scholes for stock options granted under the Stock Plan. Stock-based compensation expense for the three months ended March 31, 2014, included \$90,000, related to the issuance of convertible notes for our financial advisor.

The following table sets forth a summary of restricted stock activity for the three months ended March 31, 2015:

	Number of Restricted Shares	Weighted-Average Grant Date Fair Value
Outstanding and not vested beginning balance as of January 1, 2015	7,186	\$ 2.16
Granted	—	\$ —
Forfeited/cancelled	—	\$ —
Released/vested	(7,186)	\$ 2.16
Outstanding and not vested as of March 31, 2015	—	\$ —

Restricted stock is valued at the grant date fair value of the common stock and expensed over the requisite service period or vesting period. We estimate forfeitures when recognizing stock-based compensation expense for restricted stock, and the estimate of forfeitures is adjusted over the requisite service period should actual forfeitures differ from such estimates. As of December 31, 2014, there was approximately \$1,000, respectively, of unrecognized stock-based compensation expense associated with the granted of unvested restricted stock. Stock-based compensation expense relating to these restricted shares is being recognized over a weighted-average period of 0.2 years. The total fair value of shares vested during the three months ended March 31, 2015 and 2014, was approximately \$23,000 and \$13,000, respectively. Tax benefits resulting from tax deductions in excess of the compensation cost recognized (excess tax benefits) are classified as financing cash flows on our consolidated statements of cash flows. During the three months ended March 31, 2015 and 2014, there were no excess tax benefits relating to restricted stock and therefore there is no impact on the accompanying consolidated statements of cash flows.

The following table sets forth a summary of stock option activity for the three months ended March 31, 2015:

	Number of Shares Subject to Option	Weighted-Average Exercise Price
Outstanding as of January 1, 2015	37,034,483	\$ 0.03
Granted		—\$
Forfeited/cancelled/expired		—\$
Exercised		—\$
Outstanding as of March 31, 2015	37,034,483	\$ 0.03
Exercisable as of March 31, 2015	7,321,779	\$ 0.07

Stock options are valued at the estimated fair value grant date or the measurement date and expensed over the requisite service period or vesting period. The weighted-average volatility was based upon the historical volatility of our common stock price. There were no stock options granted during the three months ended March 31, 2015 and 2014.

The weighted-average remaining contractual term for the stock options outstanding (vested and expected to vest) and exercisable as of March 31, 2015 and December 31, 2014, was 4.1 years and 4.4 years, respectively. The total estimated fair value of stock options vested during the three months ended March 31, 2015 and 2014 was approximately \$23,000 and \$13,000, respectively. The aggregate intrinsic value of stock options outstanding as of March 31, 2015 was zero.

We estimate forfeitures when recognizing stock-based compensation expense for stock options and the estimate of forfeitures is adjusted over the requisite service period should actual forfeitures differ from such estimates. As of March 31, 2015 and December 31, 2014, there was approximately \$479,000 and \$91,000, respectively, of unrecognized stock-based compensation expense associated with stock options granted. Stock-based compensation expense relating to these stock options is being recognized over a weighted-average period of 4.3 years. Tax benefits resulting from tax deductions in excess of the compensation cost recognized (excess tax benefits) is classified as financing cash flows on our consolidated statements of cash flows. During the three ended March 31, 2015, there were no excess tax benefits relating to stock options and therefore there is no impact on the accompanying consolidated statements of cash flows.

12. Stock Warrants and Warrant Liability

On December 19, 2013 and February 25, 2014, we entered into securities purchase agreements with certain institutional accredited investors relating to the sale and issuance of a (i) convertible notes in the principal amount of \$250,000, \$200,000 and \$300,000 that mature on December 19, 2015, February 25, 2016 and March 19, 2016, respectively and (ii) five- year warrants (with a cashless exercise feature under certain circumstances) to purchase 6,250,000, 5,000,000 and 7,500,000 shares, respectively, of our common stock at an exercise price of \$0.02 per share, subject to adjustment under certain circumstances. See Note 8 for further discussion of the issuance of the convertible note.

The following table summarizes the Warrant activity for the three months ended March 31, 2015:

	Warrants for Number of Shares	Weighted-Average Exercise Price
Outstanding at January 1, 2015	22,148,045	\$ 0.23
Issued	—	—
Exercised	—	—
Cancelled/expired	—	—
Outstanding at March 31, 2015	22,148,045	\$ 0.23

The majority of our warrants outstanding are not exercisable for nine months from the date of issuance and are exercisable for either 4.5 years or 5 years thereafter. Our outstanding warrants expire on various dates between December 2015 and March 2019.

13. Earnings Per Share

On January 1, 2009, we adopted Accounting Standards Codification 260 (formerly Financial Accounting Standards Board Staff Position (“FSP”) Emerging Issues Task Force (“EITF 03-6-1”) (“ASC 260”), Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities (the “Staff Position”), which states that unvested share-based payment awards that contain non-forfeitable rights to dividends or dividend equivalents are considered participating securities and shall be included in the computation of net income (loss) per share pursuant to the two-class method described in ASC 260 (formerly Statement of Financial Accounting Standards (“SFAS”) No. 128), Earnings Per Share .

In accordance with the ASC 260, basic net income (loss) per share is computed by dividing net income (loss), excluding net income (loss) attributable to participating securities, by the weighted average number of shares outstanding less the weighted average unvested restricted shares outstanding. Diluted net income (loss) per share is computed by dividing net income (loss), excluding net income (loss) attributable to participating securities, by the denominator for basic net income (loss) per share and any dilutive effects of stock options, restricted stock, convertible notes and warrants.

	Three Months Ended March 31,	
	2015	2014
Basic:		
Numerator:		
Net loss	\$ (825,176)	\$ (84,396)
Preferred deemed dividend and preferred stock dividend		
Less: Net loss allocated to participating securities	8	960
	\$ (825,168)	\$ (83,436)
Denominator:		
Weighted-average shares outstanding	328,001,069	132,940,312
Weighted-average unvested restricted shares outstanding	(3,322)	(1,512,311)
Denominator for basic net loss per share	327,997,747	131,428,001
Basic net loss per share attributable to common stockholders	\$ (0.00)	\$ (0.00)

The following table sets forth potential shares of common stock at the end of each period presented that are not included in the calculation of diluted net loss per share because to do so would be anti-dilutive:

	March 31, 2015	December 31, 2014
Stock options outstanding	37,034,483	37,034,483
Unvested restricted stock	—	7,186
Warrants to purchase common stock	22,148,045	22,148,045

14. Concentration of Risk

Supplier Relationships

We began receiving product from Tianwei in February 2014 and stopped as of June 2014. In July 2014, we entered into a supply agreement for assembly of our proprietary modules with Auxin Solar, Inc., a panel supplier located in the United States. We began receiving product from Auxin in December 2014. Although we believe we can find alternative suppliers for solar panels manufactured to our specifications, our operations would be disrupted unless we are able to rapidly secure alternative sources of supply, our inventory and revenue could diminish significantly, causing disruption to our operations.

Historically, we obtained virtually all of our solar panels from Suntech and Lightway. During 2012, because of our cash position and liquidity constraints, we were late in making payments to both of these suppliers. On March 30, 2012, pursuant to our Supply Agreement with Lightway, we issued 1,900,000 shares of our common stock to Lightway in partial payment of our past due account payable to them. At the time of issuance, the shares were valued at \$1,045,000. On May 1, 2012, Suntech filed a complaint for breach of contract, goods sold and delivered, account stated and open account against us in the Superior Court of the State of California, County of San Francisco. Suntech alleged that it delivered products and did not receive full payment from us. On July 31, 2012, we and Suntech entered into a settlement of this dispute. Because of our inability to make scheduled settlement payments, on March 15, 2013, Suntech entered a judgment against us in the amount of \$946,438. As of March 31, 2015, Suntech has not sought to enforce its judgment. As of March 31, 2015, we have included in accounts payable in our consolidated balance sheets a balance due to Suntech America of \$946,438. We currently have no unshipped orders from Suntech or Lightway.

Customer Relationships

The relative magnitude and the mix of revenue from our largest customers have varied significantly quarter to quarter. During the three months ended March 31, 2015, three customers have accounted for significant revenues, varying by period, to our company: Smart Energy Today (“Smart Energy”), which specializes in helping home owners and business owners become more energy efficient, Helco Electrics (“Helco”) a full-service provider of electrical services in southern Oregon, Verengo Solar (“Verengo”), a solar installer based in Southern California, Sustainable Environmental Enterprises (“SEE”), a leading provider of renewable energy and development projects located in New Orleans, Louisiana, and Shoreline Electric (“Shoreline”) a provider of residential and commercial electrical services in Southern California. For the three months ended March 31, 2015 and 2014, the percentages of sales of our top five customers are as follows:

	Three Months Ended	
	March 31,	
	2015	2014
Smart Energy Today	34.9%	—
Helco Electric	12.7%	22.9%
Verengo Solar	13.9%	—
Sustainable Environmental Enterprises	—	11.7%
Shoreline Electric	—	31.9%

The percentage of our gross accounts receivable for our top accounts receivable balance as of March 31, 2015 and December 31, 2014, are as follows:

	March 31, 2015	December 31, 2014
WDC Solar, Inc.	62.4%	40.1%
Lowe's Retail	11.6%	16.8%
Greg Teegarden	11.4%	—
Sustainable Environmental Enterprises	—	6.5%

We maintain reserves for potential credit losses and such losses, in the aggregate, have generally not exceeded management's estimates. Our top three vendors accounted for approximately 30% and 39% of purchases as of March 31, 2015 and December 31, 2014, respectively. As of March 31, 2015 and December 31, 2014, accounts payable included amounts owed to our top three suppliers of approximately \$68,000 and \$0, respectively.

15. Fair Value Measurement

We use a fair-value approach to value certain assets and liabilities. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or liability. We use a fair value hierarchy, which distinguishes between assumptions based on market data (observable inputs) and an entity's own assumptions (unobservable inputs). The hierarchy consists of three levels:

- Level one — Quoted market prices in active markets for identical assets or liabilities;
- Level two — Inputs other than level one inputs that are either directly or indirectly observable; and
- Level three — Unobservable inputs developed using estimates and assumptions, which are developed by the reporting entity and reflect those assumptions that a market participant would use.

Determining which category an asset or liability falls within the hierarchy requires significant judgment. We evaluate our hierarchy disclosures each quarter. Assets and liabilities measured at fair value on a recurring basis are summarized as follows:

Liabilities	Level 1	Level 2	Level 3	December 31, 2014
Fair value of derivative liability – embedded conversion feature	\$	—\$	—\$ 129,598	\$ 129,598
Total	\$	—\$	—\$ 129,598	\$ 129,598

On August 30, 2013, November 25, 2013 and December 19, 2013, we entered into securities purchase agreements relating to the sale and issuance of convertible notes in the principal amounts of \$200,000, \$200,000 and \$250,000. Each of the Convertible Notes are convertible into shares of our common stock, at any time after issuance, at the option of the purchaser, at a conversion price equal to \$0.02, subject to adjustment upon the happening of certain events, including stock dividends, stock splits and the issuance of common stock equivalents at a price below the conversion price. Subject to our fulfilling certain conditions, including beneficial ownership limits, the convertible notes are subject to a mandatory conversion if the closing price of our common stock for any 20 consecutive days

commencing six months after the issue date of the convertible notes equal or exceeds \$0.04 per share. The terms of the convertible notes meet the criteria for the bifurcation of an embedded derivative. Therefore, we recorded the fair value of the embedded derivative liability as of the issuance date for each of the convertible notes for an aggregate fair value of \$243,889.

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We use a model based on Monte Carlo simulation to value the embedded conversion feature of our notes payable that are subject to fair value liability accounting. The determination of the fair value as of the reporting date is affected by our stock price as well as assumptions regarding a number of highly complex and subjective variables. These variables include, but are not limited to, expected stock price volatility over the term of the security and risk-free interest rate. In addition, the model uses multiple Monte Carlo simulations requiring the input of an expected life for the securities for which we have estimated and expectations of the timing and amount of future financing we may require. The fair value of the embedded conversion feature liability is revalued each balance sheet date utilizing our Monte Carlo simulation-based model computations with the decrease or increase in fair value being reported in the statement of comprehensive loss as other income or expense, respectively. The primary factors affecting the fair value of the embedded conversion feature liability are our stock price and volatility. In addition, the use of a Monte Carlo simulation-based model requires the input of highly subjective assumptions, and other reasonable assumptions could provide differing results.

During the quarter ended March 31, 2015, the Monte Carlo Simulation-based model was used to calculate the fair value of the embedded conversion feature based on a stock price of between \$0.011 and \$0.036 and a volatility of between 94.4% and 99.7%.

The following table shows the changes in Level 3 liabilities measured at fair value on a recurring basis for the three months ended March 31, 2015:

	Derivative Liability – Embedded Conversion Feature	Total Level 3
Beginning balance – January 1, 2015	\$ 129,598	\$ 129,598
Issuances	—	—
Conversions	(88,333)	(88,333)
Total realized and unrealized gains or losses	(41,265)	(41,265)
Ending balance – March 31, 2015	\$ —	\$ —

16. Income Taxes

Deferred income taxes arise from timing differences resulting from income and expense items reported for financial account and tax purposes in different periods. A deferred tax asset valuation allowance is recorded when it is more likely than not that deferred tax assets will not be realized. During the three months ended March 31, 2015, there was no income tax expense or benefit for federal and state income taxes in the accompanying condensed consolidated statements of operations due to our net loss and a valuation allowance on the resulting deferred tax asset. Our deferred tax asset has a 100% valuation allowance.

17. Commitments and Contingencies

Litigation

On February 9, 2015, the law firm of Snell & Wilmer LLP filed suit against us in California Superior Court, County of Orange. The complaint alleges that we have failed to pay Snell & Wilmer fees due to that firm in connection with prior patent prosecution litigation, in an amount of no less than \$808,202, plus interest. We are still evaluating the merits of the claim but intend to defend against it vigorously.

We are also involved in other litigation from time to time in the ordinary course of business. In the opinion of management, the outcome of such proceedings will not materially affect our financial position, results of operations or cash flows.

18. Subsequent Events

On April 6 and April 20, 2015, we received proceed of approximately \$55,000 and \$94,000 related to the sale of approximately 14 million shares under our Equity Purchase Agreement. On April 1, 2015, we issued 24 million shares of our common stock pursuant to a put notice under the Equity Purchase Agreement.

On April 17, 2015, we entered into a sublease for 1,500 square feet of office space and 2,000 square feet of warehouse storage space at 48900 Milmont Drive, Fremont, California, for \$4,250 per month. The lease began when we initially occupied the new facilities on May 8, 2015 and the term will run for 12 months, expiring on May 30, 2016, after which it will be month-to-month.

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