Mill City Ventures III, Ltd
Form 10-Q
May 12, 2015

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q

x QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 2015 OR

o TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from______ to _________

Commission File Number 814-00991

MILL CITY VENTURES III, LTD.

(Exact name of registrant as specified in its charter)

Minnesota	90-0316651
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

328 Barry Avenue South #210, Wayzata, MN 55391

(Address of Principal Executive Offices)

(952) 479-1923

(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed from last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ¨ No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ¨	Accelerated filer ¨
Non-accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company x

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x

As of March 31, 2015, there were 12,151,493 shares of the issuer's common stock, \$0.001 par value, outstanding.

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PART I – FINANCIAL INFORMATION

Item 1. Financial Statements

Mill City Ventures III, Ltd.

Balance Sheets

	March 31, 2015 (unaudited)	December 31, 2014 (audited)
ASSETS		
Investments, at fair value		
Non-control / Non-affiliate investments (cost of $7,314,965 and $5,797,518, respectively)	$ 8,694,679	$ 7,171,509
Cash	2,783,237	4,105,911
Prepaid expenses	25,414	49,623
Receivable from sale of investments	40,185	82,103
Interest and dividends receivable	100,547	59,794
Leasehold improvements, net	29,855	31,882
Property and equipment, net	17,777	18,962
Total Assets	$ 11,691,694	$ 11,519,784
LIABILITIES		
Current Liabilities		
Accounts payable	$ 26,442	$ 36,098
Deferred interest income	28,145	-
Deferred rent	10,238	9,996
Total Current Liabilities	64,825	46,094
Total Liabilities	64,825	46,094
SHAREHOLDERS' EQUITY		
Common Stock, par value $0.001 per share (250,000,000 common shares authorized; 12,151,493 and 12,151,493 issued and outstanding)	12,151	12,151
Additional paid-in capital	11,857,660	11,857,660
Accumulated deficit	(1,159,665)	(1,159,665)
Accumulated undistributed investment loss	(1,027,820)	(1,028,423)
Accumulated undistributed net realized gains on investment transactions	564,829	417,976
Net unrealized appreciation in value of investments	1,379,714	1,373,991

Total Shareholders' Equity	11,626,869	11,473,690
Total Liabilities and Shareholders' Equity	$ 11,691,694	$ 11,519,784
Net Asset Value Per Common Share	$ 0.95	$ 0.94

See accompanying notes to financial statements.

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Mill City Ventures III, Ltd.

Statement of Operations

(unaudited)

	Three Months Ended March 31, 2015	Three Months Ended March 31, 2014
Investment Income		
Interest income	$ 138,526	$ 29,466
Dividend income	25,318	12,298
Total Investment Income	163,844	41,764
Operating Expenses		
Professional fees	51,397	37,177
Payroll expense	41,474	41,446
Insurance expense	24,564	33,321
Occupancy	22,799	17,406
Directors' fees expense	15,000	15,000
Depreciation and amortization expense	3,212	3,098
Other general and administrative expenses	4,795	3,850
Total Operating Expenses	163,241	151,298
Net Investment Income (Loss)	603	(109,534)
Realized and Unrealized Gain on Investments		
Net realized gain on investments	146,853	200,903
Net change in unrealized appreciation on investments	5,723	683,197
Net Realized and Unrealized Gain on Investments	152,576	884,100
Net Increase in Net Asset Value Resulting from Operations	$ 153,179	$ 774,566
Net Increase in Net Assets Resulting from Operations per share:		
Basic and diluted	$ 0.01	$ 0.06
Weighted-average number of common shares outstanding	12,151,493	12,169,422

See accompanying notes to financial statements.

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Mill City Ventures III, Ltd.

Statements of Cash Flows

(unaudited)

	Three Months Ended March 31, 2015	Three Months Ended March 31, 2014
Cash flows from operating activities:		
Net increase in net asset value resulting from operations	$ 153,179	$ 774,566
Adjustments to reconcile net increase in net assets resulting from operations to net cash used in operating activities:		
Net change in unrealized appreciation on investments	(5,723)	(683,197)
Net realized gain on investments	(146,853)	(200,903)
Payments for purchases of investments	(1,816,399)	(1,280,000)
Proceeds from sales of investments	445,805	622,894
Depreciation and amortization expense	3,212	3,098
Changes in operating assets and liabilities:		
Prepaid expenses	24,209	(69,796)
Receivable from sale of investments	41,918	794
Interest and dividends receivable	(40,753)	3,750
Accounts payable	(9,656)	94,498
Deferred interest income	28,145	15,000
Accrued royalty	-	(619)
Deferred rent	242	562
Net cash used in operating activities	(1,322,674)	(719,353)
Cash flows from investing activities:		
Purchases of property and equipment	-	(3,943)
Purchases of leasehold improvements	-	(2,561)
Net cash used by investing activities	-	(6,504)
Net decrease in cash	(1,322,674)	(725,857)
Cash, beginning of the period	4,105,911	7,090,379
Cash, end of the period	$ 2,783,237	$ 6,364,522

See accompanying notes to financial statements.

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Mill City Ventures III, Ltd.

Financial Highlights

(unaudited)

	Three Months Ended March 31, 2015	
Per Share Data		
Net asset value at beginning of the period	$ 0.94	
Net investment income	0.00	
Net realized and unrealized gains	0.01	
Net asset value at end of period	$ 0.95	
Ratio / Supplemental Data		
Per share market value of investments at end of period	$ 0.72	
Shares outstanding at end of period	12,151,493	
Average weighted shares outstanding for period	12,151,493	
Net assets at end of period	$ 11,626,869	
Average net assets [1]	$ 11,561,049	
Portfolio turnover rate [2]	3.86	%
Ratio of operating expenses to average net assets [2]	(5.60	)%
Ratio of net investment income to average net assets [2]	0.02	%
Ratio of realized gains to average net assets [2]	5.25	%

[1] Based on the monthly average of net assets as of the beginning and end of each period presented.

[2] Ratios are annualized.

See accompanying notes to financial statements.

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Mill City Ventures III, Ltd.

Schedule of Investments

As of March 31, 2015

(Unaudited)

Portfolio Company	**Description of Securities**	**Cost**	**Fair Value**
Creative Realities Inc.	12% Convertible Promissory Note (Mat. 8/18/16)†	$1,000,000	$1,000,000
	1,515,512 $0.38 Cashless Warrants (Exp. 2/18/20)*†	-	-
BioLife Solutions	Common Stock*	107,500	40,250
	$4.70 Cashless Warrants (Exp. 3/20/21)*	-	-
Combimatrix	$1.97 Cashless Warrants (Exp. 12/29/2018)*	-	-
	$3.12 Cashless Warrants (Exp. 12/19/2018)*	-	-
Mix 1 Life Inc.	12% Convertible Promissory Note (Mat. 2/6/16)	500,000	500,000
	12% Promissory Note (Mat. 3/13/16)†	250,000	250,000
	Common Stock*	-	2,002,554
Tzfat Spirits of Israel, LLC	Class A Membership Units*†	101,019	25,000
Insite Software Solutions, Inc.	10.5% Promissory Note (Mat. 12/30/2018)	750,000	750,000
	$0.01 Warrants (Change Of Control) (Exp 12/30/23)*	-	-
MAX 4G Wireless, Inc.	Series B Convertible Preferred Stock*†	150,000	150,000
Calamos Convertible and High Income Fund	Closed End Fund	128,357	141,700
Powershares KBW High Dividend Yield Financial	ETF	253,510	254,400
Solar Senior Capital, Ltd.	Common Stock	91,983	97,417
DBR Phase III US Investors, LLC	Membership Units†	1,000,000	1,000,000
The Igloo, LLC	20% Senior Secured Note (Mat. 12/31/16)†	500,000	500,000
Discovery Communications Inc	Common Stock Series A	149,609	153,800
Dala Petroleum (aka Westcott Products)	Series A 6% Convertible Preferred Stock	500,000	500,000
	714,286 $1.35 Cashless Warrants (Exp. 6/3/17)*	-	-
Northern Capital Partners I, LP	Membership Units*†	500,000	444,208
Southern Plains Resources, Inc.	Common Stock*	730,000	300,000
Hi-Crush Partners, LP	Limited Partnership Units	183,660	175,350
AT&T Inc.	Common Stock	175,260	163,250
Century Link Inc	Common Stock	157,360	172,750
Windstream Holdings	Common Stock	86,707	74,000
	Total Investments	**$7,314,965**	**$8,694,679**

† Restricted security

* Indicates securities are not income producing

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Mill City Ventures III, Ltd.

Portfolio Investments by Industry

As of March 31, 2015

(Unaudited)

Security Name	Industry	Date of Initial Investment	Investment	Quantity or Face Value	Cost	Fair Value	% of Net Assets
Creative Realities, Inc.	Advertising	2/18/2011	Promissory Note	1,000,000	$1,000,000	$1,000,000	
Creative Realities, Inc.	Advertising	2/18/2011	Warrants	1,515,152	—	—	
					1,000,000	1,000,000	8.60 %
Bio Life Solutions, Inc.	Bio-technology	3/20/2010	Common Stock	25,000	107,500	40,250	
Bio Life Solutions, Inc.	Bio-technology	3/20/2010	Warrants	100,000	—	—	
Combimatrix Corporation	Bio-technology	5/5/2009	Warrants	413,934	—	—	
					107,500	40,250	0.35 %
Mix 1 Life, Inc.	Consumer	2/5/2010	Promissory Note	500,000	500,000	500,000	
Mix 1 Life, Inc.	Consumer	3/8/2011	Promissory Note	250,000	250,000	250,000	
Mix 1 Life, Inc.	Consumer	8/6/2010	Common Stock	324,563	—	2,002,554	
Tzfat Spirits of Israel, LLC	Consumer	10/13/2009	Membership Units	55,000	101,019	25,000	
					851,019	2,777,554	23.89%
Insite Software Solutions, Inc.	Information Technology	12/29/2009	Promissory Note	750,000	750,000	750,000	
Insite Software Solutions, Inc.	Information Technology	12/29/2009	Warrants	108,960	—	—	
MAX 4G	Information Technology	6/13/2009	Preferred Stock	300,000	150,000	150,000	
					900,000	900,000	7.74 %
Calamos Convertible &	Investment Fund	11/4/2009	Common Stock	10,000	128,357	141,700	

High Income Fund							
Powershares High Dividend Yield	Investment Fund	5/11/2010	Common Stock	10,000	253,510	254,400	
Solar Senior Capital Ltd	Investment Fund	1/15/2011	Common Stock	6,047	91,983	97,417	
					473,850	493,517	4.24 %
DBR Phase III US Investors, LLC	Leisure & Hospitality	2/6/2010	LP Units	1,000,000	1,000,000	1,000,000	
The Igloo LLC	Leisure & Hospitality	12/30/2010	Promissory Note	500,000	500,000	500,000	
					1,500,000	1,500,000	12.90 %
Discovery Communications Inc.	Media	1/22/2011	Common Stock	5,000	149,609	153,800	1.32 %
Dala Petroleum, Inc.	Oil & Gas	6/2/2010	Preferred Stock	500	500,000	500,000	
Dala Petroleum, Inc.	Oil & Gas	6/2/2010	Warrants	714,286	—	—	
HI Crush Partners	Oil & Gas	2/23/2011	Common Stock	5,000	183,660	175,350	
Northern Capital, LP	Oil & Gas	6/15/2010	Membership Units	500,000	500,000	444,208	
Southern Plains Resources, Inc.	Oil & Gas	3/13/2009	Common Stock	600,000	730,000	300,000	
					1,913,660	1,419,558	12.21 %
AT&T	Telecommunications	10/24/2009	Common Stock	5,000	175,260	163,250	
CenturyLink, Inc.	Telecommunications	10/27/2009	Common Stock	5,000	157,360	172,750	
Windstream Holdings Inc.	Telecommunications	11/5/2009	Common Stock	10,000	86,707	74,000	
					419,327	410,000	3.53 %
Total Investments					$7,314,965	$8,694,679	74.78 %

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Mill City Ventures III, Ltd.

Notes to Financial Statements

March 31, 2015

NOTE 1—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Description of Operations and Basis of Presentation

Mill City Ventures III, Ltd. (the "Company") is an investment company that was incorporated in the State of Minnesota on January 10, 2006 under the name WPP Acquisition, Inc. The Company's name was subsequently changed to Poker Magic, Inc. Our business from January 10, 2006 (inception) through December 12, 2012 consisted primarily of marketing and licensing a new form of poker-based table game to casinos and on-line gaming facilities in the United States.

On December 13, 2012, we filed a Form N-8A with the SEC, notifying the SEC that we intended to convert the Company to an internally managed, non-diversified, closed-end investment company under the Investment Company Act of 1940 (the "1940 Act"). On February 7, 2013, we filed Form N-54A, notifying the SEC of our election to become a business development company ("BDC"). Subsequently, on May 13, 2013, we filed Form N-8F to deregister as a registered investment company based upon our prior filing to become a BDC. On September 25, 2013, the SEC issued an order under Section 8(f) of the Investment Company Act of 1940 declaring that the Company has ceased to be an investment company. We are regulated as a BDC and plan to be taxed as a regulated investment company, although we currently have not elected this tax status. As a BDC, we primarily focus on investing in or lending to privately held and publicly traded companies and making managerial assistance available to such companies. A BDC may provide shareholders with the ability to retain the liquidity of a publicly traded stock, while sharing in the possible benefits of investing in emerging-growth or expansion-stage companies. Our future revenues will relate to the earnings we receive from the sale of securities, dividends and interest from our portfolio investments. The Company's objective is to obtain returns from investments in securities and other investment opportunities available to business development companies under the 1940 Act. We intend to invest capital in portfolio companies for purposes of financing acquisitions, recapitalizations, buyouts, organic growth and working capital. Buyouts generally include transactions that involve the acquisition of a controlling interest in an entity, either by management or other investors. Organic growth refers to growth through the internal operations of the company, through investments in marketing initiatives, capital expenditures or other internal growth initiatives, rather than growth by means of an acquisition. We plan to identify potential investments through multiple sources, including private equity sponsors, investment bankers, brokers, and owners and operators of businesses. We will base our investment decisions on analyses of potential customers' business operations and asset valuations as well as financing structure, utilizing risk management methods, pricing tools, due diligence methodologies and data management processes designed to help us assess risk, establish appropriate pricing, and maximize our return on investment. Subject to regulations set forth in the 1940 Act and applicable to BDCs, we plan to invest in private companies, small-cap public stocks, notes and other forms of debt, investment contracts, and other investments commonly referred to as securities.

On January 17, 2013, the Company amended and restated our Articles of Incorporation. The amendment and restatement included a change in our name from "Poker Magic, Inc." to "Mill City Ventures III, Ltd."

On February 7, 2013, the Company filed Form N-54A, Notification of Election to be Subject to Sections 55 through 65 of the Investment Company Act of 1940 notifying the SEC that we are closed-end company that will be operated for the purpose of making investments primarily in securities described in section 55(a)(1) through (3) of the Investment Company Act of 1940 and will make available significant managerial assistance with respect to issuers of such securities to the extent required by the Act.

Interim Financial Information

The balance sheet as of December 31, 2014, which has been derived from audited financial statements, and the unaudited interim condensed financial statements have been prepared in accordance with accounting principles generally accepted in the United States and pursuant to the rules and regulations of the Securities and Exchange Commission (the “SEC”) for interim financial information. Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States have been omitted pursuant to such rules and regulations. Operating results for the three months ended March 31, 2015 are not necessarily indicative of the results that may be expected for the year ending December 31, 2015 or any other period. The accompanying financial statements and related notes should be read in conjunction with our audited financial statements and notes thereto contained in our Annual Report on Form 10-K for the year ended December 31, 2014. The financial information furnished in this report is unaudited and reflects all adjustments which are normal recurring adjustments and, which in the opinion of management, are necessary to fairly present the results of the interim periods presented in order to make the financial statements not misleading.

Use of Estimates

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

Cash Deposits

The Company maintains its cash balances in financial institutions and with regulated financial investment brokers. Cash on deposit in excess of FDIC and similar coverage is subject to the usual banking risk of funds in excess of those limits.

Fair Value of Financial Instruments

The carrying amounts of certain of the Company’s financial instruments, including cash, receivable from sale of investments, interest and dividends receivable, prepaid expenses, accounts payable and notes payable approximate fair value due to their relatively short maturities.

In the normal course of business, the Company may utilize derivative financial instruments (principally options) in connection with its trading activities. The Company records its derivative activities at fair value. Gains and losses from derivative financial instruments are included in net gain (loss) on investments in the statement of operations.

Investment Valuation

Investment transactions are recorded on the trade date. Realized gains or losses on investments are measured by the difference between the net proceeds from the repayment or sale and the amortized cost basis of the investment without regard to unrealized gains or losses on investments previously recognized, and include investments charged off during the period, net of recoveries. Unrealized gains or losses on investments primarily reflect the change in investment values, including the reversal of previously recorded unrealized gains or losses when gains or losses are realized.

Investments for which market quotations are readily available are typically valued at such market quotations. In order to validate market quotations, we look at a number of factors to determine if the quotations are representative of fair value, including the source and nature of the quotations. Debt and equity securities that are not publicly traded or whose market prices are not readily available are valued at fair value as determined in good faith by our Board of Directors or the Valuation Committee of the board, based on, among other things, the input of our executive management, audit committee and independent third-party valuation expert that may be engaged by management to assist in the valuation of our portfolio investments, but in all cases consistent with our written valuation policies and procedures.

Due to the inherent uncertainty of determining the fair value of investments that do not have a readily available market value, the fair value of our investments may fluctuate from period to period. Additionally, the fair value of our investments may differ significantly from the values that would have been used had a ready market existed for such investments and may differ materially from the values that we may ultimately realize. Further, such investments are generally less liquid than publicly traded securities. If we were required to liquidate a portfolio investment in a forced or liquidation sale, we could realize significantly less than the value at which we have recorded it.

In addition, changes in the market environment and other events that may occur over the life of the investments may cause the gains or losses ultimately realized on these investments to be different than the unrealized gains or losses reflected in the valuations currently assigned.

Allocation of Net Gains and Losses

All income, gains, losses, deductions and credits for any investment are allocated in a manner proportionate to the shares owned.

Income Taxes

The Company accounts for income taxes under the liability method. Under this method, deferred tax assets and liabilities are determined based on the difference between the financial statement and tax bases of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to affect taxable income. Valuation allowances are established when necessary to reduce deferred tax assets to the amounts expected to be realized.

Realized Gains and Losses, Interest and Dividend Income Recognition

Realized gains or losses on the sale of investments are calculated using the specific investment method.

Interest income is recorded on an accrual basis and includes the accretion of discounts and amortization of premiums. Discounts from and premiums to par value on securities purchased are accreted/amortized into interest income over the life of the respective security using the effective yield method. The amortized cost of investments represents the original cost adjusted for the accretion of discounts and amortization of premiums, if any.

Loans are generally placed on non-accrual status when principal or interest payments are past due 30 days or more or when there is reasonable doubt that principal or interest will be collected in full. Accrued and unpaid interest is generally reversed when a loan is placed on non-accrual status. Interest payments received on non-accrual loans may be recognized as income or applied to principal depending upon management's judgment regarding collectability. Non-accrual loans are restored to accrual status when past due principal and interest is paid and, in management's judgment, are likely to remain current. The Company may make exceptions to this if the loan has sufficient collateral value and is in the process of collection.

Dividend income on preferred equity securities is recorded as dividend income on an accrual basis to the extent that such amounts are payable by the portfolio company and are expected to be collected. Dividend income on common equity securities is recorded on the record date for private portfolio companies or on the ex-dividend date for publicly traded portfolio companies.

Our investment portfolio investments at March 31, 2015 and December 31, 2014 were $8,694,679 and $7,171,509, respectively.

Management and Service Fees

The Company does not incur expenses related to management and service fees. Our executive management team manages the Company's investments as part of their employment responsibilities.

Recent Accounting Pronouncements

No other new accounting pronouncement issued or effective during the fiscal quarter has had or is expected to have a material impact on the condensed financial statements.

NOTE 2—NET GAIN (LOSS) PER COMMON SHARE

Basic net gain (loss) per common share is computed by dividing net gain (loss) by the weighted average number of vested common shares outstanding during the period. A reconciliation of the numerator and denominator used in the calculation of basic and diluted net gain (loss) per common share follows:

	For the Three Months Ended March 31,	
	2015	2014
Numerator: Net Increase in Net Asset Value Resulting from Operations	$ 153,179	$ 774,566
Denominator: Weighted-average number of common shares outstanding	12,151,493	12,169,422
Basic and diluted net gain (loss) per common share	$ 0.01	$ 0.06

At March 31, 2015 and 2014, the Company did not have any options or warrants outstanding or any other dilutive common equivalent shares.

NOTE 3—COMMITMENTS AND CONTINGENCIES

The Company has an agreement to lease approximately 1,917 square feet of commercial space and two parking spots, for a period of 62 months. The 62-month lease term began October 1, 2013 and runs through November 30, 2018. The total rent expense for the three -month period ended March 31, 2015 was $22,799.

The following is a schedule of the required annual minimum lease payments.

Year	**Amount**
2015	33,148
2016	46,179
2017	50,311
2018	46,988
TOTAL	$176,626

NOTE 4—SHAREHOLDERS' EQUITY

Common stock

On August 29, 2014 we purchased and retired 2,973 shares of common stock at a per-share price of $0.83.

On September 3, 2014, we purchased and retired 4,510 shares of common stock at a per-share price of $0.80.

On December 19, 2014, we purchased and retired 10,446 shares of common stock at a per-share price of $0.84.

At March 31, 2015, a total of 12,151,493 shares of common stock were issued and outstanding.

NOTE 5—FAIR VALUE OF INVESTMENTS

Investment Risks

The Company’s investments are subject to a variety of risks. Those risks include the following:

Market Risk

Market risk represents the potential loss that can be caused by a change in the fair value of the instrument.

Credit Risk

Credit risk represents the risk that the Company would incur if the counterparties failed to perform pursuant to the terms of their agreements with the Company.

Fair Value Hierarchy

The fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three broad levels is explained below:

Level 1

Valuations based on unadjusted quoted prices in active markets for identical assets or liabilities that we have the ability to access. Valuation adjustments are not applied to Level 1 securities. Because valuations are based on quoted prices that are readily and regularly available in an active market, valuation of these securities does not entail a significant degree of judgment.

Level 2

Pricing inputs are other than used in Level 1, which include the closing bid price for unlisted marketable securities, which are available in active or inactive markets for identical investments or liabilities, other direct or indirect observable inputs that can be corroborated by market data or the use of models or other valuation methodologies as of the reporting date.

Level 3

Pricing inputs are unobservable for the investment and include situations where there is little, if any, market activity for the investment. The inputs into the determination of fair value require significant management judgment or estimation.

The table below presents the balances of assets measured at fair value within respective industries.

	As of March 31, 2015			
	Level 1	**Level 2**	**Level 3**	**Total**
AT&T	$163, 250	$ -	$-	$**163, 250**
Calamos Convertible & High Income Fund	141,700	-	-	141,700
CenturyLink, Inc.	172,750	-	-	172,750
Discovery Communications Corp.	153,800	-	-	153,800
Hi Crush Partners, LP	175,350	-	-	175,350
Windstream Holdings, Inc.	74,000	-	-	74,000
BioLife Solutions, Inc.	40,250	-	-	40,250
Solar Senior Capital Ltd	97,417	-	-	97,417
Powershares High Yield Dividend Fund	254,400	-	-	254,400
Southern Plains Resources, Inc.	-	-	300,000	300,000
Max 4G	-	-	150,000	150,000
Tzfat Spirits of Israel, LLC	-	-	25,000	25,000
Insite Software Solutions, Inc.	-	-	750,000	750,000
DBR Phase III US Investors, LLC	-	-	1,000,000	1,000,000
Mix 1 Life, Inc. Convertible Note	-	-	500,000	500,000
Mix 1 Life, Inc. Promissory Note	-	-	250,000	250,000
Mix 1 Life, Inc. Common Stock	2,002,554	-	-	2,002,554
Dala Petroleum (aka Westcott Products Corp)	-	-	500,000	500,000
The Igloo, LLC	-	-	500,000	500,000
Creative Realities, Inc.	-	-	1,000,000	1,000,000
Northern Capital Partners I, LP	-	-	444,208	444,208

Total	$3,275,471	$ -	$5,419,208	$8,694,679

The changes in Level 3 assets and liabilities measured at fair value on a recurring basis are summarized as follows:

	Fair Value
Fair value, December 31, 2014	$4,225,000
Change in unrealized appreciation	(55,792)
Net realized and unrealized gain	(55,792)
Purchases of portfolio investments	1,250,000
Fair value, March 31, 2015	$5,419,208
Net unrealized gains included in the net increase in net assets resulting from operations relating to assets held at March 31, 2015	$(55,792)

Portfolio Investments

At March 31, 2015, we held investments in 12 eligible portfolio investments, which had an amortized cost of $6,088,519 and a fair value of $7,462,012. At December 31, 2014, we held investments in 11 eligible portfolio investments, which had an amortized cost of $4,946,019 and a fair value of $6,265,399.

On March 1, 2013, we entered into a subscription agreement with Great Plains Sand, LLC through a private placement of common stock for the purchase of 1 Class A Membership Unit for $105,000. On May 24, 2013, Great Plains Sand, LLC sold its company to Fairmount Minerals, Ltd. for a sale price of $65 million subject to certain adjustments for the final working capital settlement and the retention of a limited amount of the sale consideration to pay certain post-closing expenses. After expenses, we received approximately $182,176 in cash with the potential of an additional $18,750 in escrow to be paid within 60 days of closing and a potential earnout of $18,750 to be paid within one year of closing. On February 25, 2014, $7,500 was received in satisfaction of post-closing payment rights under the acquisition agreement. On August 7, 2014 an additional $28,000 was received and on December 31, 2014 $258 was received in final satisfaction of post-closing payment rights under the acquisition agreement.

On March 6, 2013, we entered into a purchase and sale agreement with Mill City Ventures II, LP, wherein we purchased 400,000 shares of Southern Plains Resources, Inc. common stock from Mill City Ventures II, LP for $420,000. On July 11, 2013, the Company entered into a subscription agreement with Southern Plains Resources, Inc. through a private placement of common stock to purchase an additional 200,000 shares of common stock at $1.55 per share for $310,000. Our cost of the Southern Plains investment at March 31, 2015 was $730,000 and the fair value was $300,000.

On May 3, 2013, we entered into a securities purchase agreement with CombiMatrix Corporation ("CombiMatrix") to purchase Series C Convertible Preferred Stock and warrants in two separate closings. In the May 6, 2013 closing, we purchased 200 shares of Series C preferred stock convertible into common stock at $2.86 per share and 81,967 warrants with an exercise price of $3.77 per share. In the June 28, 2013 closing, we purchased 200 shares of Series C preferred stock convertible into common stock at $2.86 per share and 81,967 warrants with an exercise price of $3.55 per share. On August 9, 2013, we converted 100 shares of the CombiMatrix 6% Series C shares to 34,994 shares of CombiMatrix common stock at $2.86 per share. An additional 207 shares of common stock were issued in lieu of accrued dividend on the converted principal amount. Our cost for the CombiMatrix investment was $400,600 and the fair value at September 30, 2013 was $400,675. On November 21, 2013, we converted 300 shares of the CombiMatrix 6% series C shares to 104,983 shares of CombiMatrix common stock at $2.86 per share. An additional 3,710 shares of common stock were issued in lieu of accrued dividend on the converted principal balance. On December 18, 2013, we purchased 515 Series D Convertible preferred shares of CombiMatrix Corporation for $1,000 per share for a total purchase price of $515,000 with a warrant to purchase 250,000 shares of common stock at $3.12. Each Series D Convertible share is convertible into common stock at $2.06 per share. The warrant has an expiration date of December 18, 2018. On December 19, we converted 515 Series D Convertible preferred shares into 250,000 shares of common stock. During the first quarter ended March 31, 2014, we sold 204,850 shares of the common stock for $615,394, resulting in a realized gain of $193,403. During the third quarter ended September 30, 2014, we sold the remaining 45,150 shares of the common stock for $61,252, resulting in a realized loss of $31,756. On February 13, 2015, CombiMatrix modified the conversion price of the 81,967 warrants at $3.77 and the 81,967 warrants at $3.55 to a $1.97 conversion price for the duration of the life of the warrants. The modification was made in accordance with anti-dilution price-protection provisions in the warrant. At March 31, 2015 the cost and fair value of the warrants was $0.

On May 29, 2013, we entered into a subscription and investment letter with MAX4G, Inc. to purchase 300,000 shares of MAX4G's Series B Convertible Preferred Stock, $.001 par value per share, at $0.50 per share, for a total of $150,000. At March 31, 2015, the cost and fair value of the MAX4G investment was $150,000.

On October 14, 2013, we entered into subscription agreement with Tzfat Spirits of Israel, LLC, to purchase 55,000 Class A Membership Units at $1.8367 per unit for a total of $101,019. At March 31, 2015, the cost and fair value of the Tzfat investment was $101,019 and $25,000, respectively.

On December 30, 2013, we entered into a Promissory Note and Warrant Purchase Agreement with Insite Software Solutions, Inc. and in connection therewith purchased a $750,000 promissory note and received a warrant to purchase

108,960 shares of Insite Software common stock at one cent ($0.01) per share. The warrant has a 10-year term expiring December 30, 2023. At March 31, 2015, the cost and fair value of the promissory note was $750,000 and the warrant was $0.

On February 6, 2014, we entered into a Senior Secured Convertible Promissory Note and Warrant Purchase Agreement with Mix 1 Life, Inc. and in connection therewith purchased a $500,000 senior secured convertible promissory note and received a warrant to purchase up to 1,600,000 shares of Mix 1 Life common stock at $0.50 per share. The note currently is convertible into shares of common stock at $1.08 per share (post split). The warrant has a five-year term expiring February 6, 2019. On August 7, 2014 we elected to exercise, on a cashless basis, our warrants into 1,121,912 shares of common stock. On September 11, 2014, a 1-for-3 reverse split on those common shares reduced our holdings to 373,971 common shares. At March 31, 2015, the cost and fair value of the promissory note was $500,000 and the cost and fair value of the common stock was $0 and $2,002,554, respectively. Our director Mr. Larson is currently the Chief Financial Officer, director and 5% shareholder of Mix 1 Life, Inc. Mr. Larson was appointed Chief Financial Officer and a director of Mix 1 on June 24, 2014, after our initial investment in Mix 1 Life.

On February 7, 2014, we entered into a Purchase Agreement for $1,000,000 of limited liability company interests with DBR Phase III US Investors, LLC and in connection therewith funded a first capital call of $350,000. A second capital call of $350,000 was funded on May 9, 2014 and the final capital call was funded on October 21, 2014 in the amount of $300,000. At March 31, 2015, the cost and fair value of the interests was $1,000,000.

On June 3, 2014, we entered into a subscription and warrant purchase agreement with Dala Petroleum Corporation (fka Westcott Products Corporation) to purchase 500 shares of Series A 6% Convertible Preferred Stock, $.01 par value per share, at $1,000 per share, for a total of $500,000 and received a warrant to purchase up to 714,286 shares of Dala Petroleum common stock at $1.35 per share. The preferred stock converts into common stock at $0.70. The warrant has a three-year term, expiring June 3, 2017. At March 31, 2015, the cost and fair value of the preferred stock was $500,000 and the cost and fair value of the warrant was $0.

On May 16, 2014, we entered into a Purchase Agreement for $500,000 of limited partnership interests with Northern Capital Partners I, LP and in connection therewith funded a first capital call of $50,000 on June 16. A second capital call of $125,000 was funded on August 26, 2014, a third capital call of $200,000 was funded on October 21, 2014 and the fourth and final capital call of $125,000 was funded on December 26, 2014. At March 31, 2015, the cost and fair value of the interests was $500,000 and $444,208, respectively.

On December 31, 2014, we entered into a Promissory Note Agreement for $500,000 with The Igloo, LLC and in connection therewith funded a $500,000 promissory note. At March 31, 2015, the cost and fair value of the note was $500,000.

On February 19, 2015, we purchased a 12% convertible note from Creative Realities, Inc. for $1,000,000 principal amount. The note bears 12% annual interest paid monthly in arrears and is due August 18, 2016. The outstanding principal amount is convertible into common stock at $0.33. In conjunction with the financing, we received a warrant to purchase 1,515,152 common shares with a conversion price of $0.38. The warrant has a cashless conversion provision and expires February 17, 2020. At March 31, 2015, the cost and fair value of the note was $1,000,000. The cost and value of the warrant is $0.

On March 13, 2015, we purchased a 12% senior secured promissory note from Mix 1 Life, Inc. for $250,000 principal amount. At closing, 12 months of interest was prepaid by Mix 1. The note is due on March 13, 2016. Our director Christopher Larson is also a director and the Chief Financial Officer of Mix 1 Life as well as a 5% shareholder in Mix 1. At March 31, 2015, the cost and fair value of the note was $250,000.

NOTE 6—MINIMUM ASSET COVERAGE

As a BDC, we are required to meet various regulator tests. Among other things, these tests will require us to invest at least 70% of our total assets in private or small-cap public U.S.-based companies, and to maintain a coverage ratio of total net assets to total senior securities and borrowings (including accrued interest payable) of at least 200%. As of March 31, 2015, approximately 86% of our investments (by fair value at that date) were in private or small-cap public U.S.-based companies and our coverage ratio was 100%.

NOTE 7—INCOME TAXES

We plan to be regulated as a regulated investment company (“RIC”) and intend to comply with the requirements of the Internal Revenue Code, applicable to regulated investment companies. Currently, we have not elected to be treated as a RIC. We are required to distribute at least 90% of our investment company taxable income and intend to distribute (or retain through a deemed distribution) all of our investment company taxable income and net capital gain to shareholders; therefore, we have made no provision for income taxes. The characterization of income and gains that we will distribute is determined in accordance with income tax regulations that may differ from GAAP. Book and tax basis differences relating to shareholder dividends and distributions and other permanent book and tax differences are reclassified to paid-in capital.

NOTE 8—SUBSEQUENT EVENTS

On April 27, 2015, Insite Software Solutions, Inc. redeemed the outstanding balance of the promissory note, $750,000, owned by the Company. In addition, accrued interest in the amount of $5,825.34 was also received.

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Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations

Our Management’s Discussion and Analysis of Financial Condition and Results of Operations set forth below should be read in conjunction with our audited financial statements, and notes thereto, contained in our Form 10-K filed with the SEC on March 31, 2015 related to our year ended December 31, 2014.

Forward-Looking Statements

Some of the statements made in this section of our report are forward-looking statements based on the current expectations of the management of our company. These expectations involve substantial risks and uncertainties which could cause actual results to differ materially from the results expressed in, or implied by, these forward-looking statements. Forward-looking statements relate to future events or our future financial performance. We generally identify forward-looking statements by terminology such as “may,” “will,” “should,” “expects,” “plans,” “anticipates,” “could,” “intends,” “targets,” “projects,” “contemplates,” “believes,” “estimates,” “predicts,” “potential” or “continue” or the negative o terms or other similar words. Important assumptions include our ability to originate new investments, achieve certain margins and levels of profitability, the availability of additional capital, and the ability to maintain certain debt-to-asset ratios. In light of these and other uncertainties, the inclusion of a projection or forward-looking statement in this report should not be regarded as a representation by us that our plans or objectives will be achieved.

Some of the forward-looking statements contained in this report include statements as to:

- our future operating results;
- our business prospects and the prospects of our portfolio companies;
- the outcome of a pending compliance inspection by the SEC Office of Compliance and Inspections;
- the impact of investments that we expect to make;
- our informal relationships with third parties;

- the dependence of our future success on the general economy and its impact on the industries in which we invest;
- the ability of our portfolio companies to achieve their objectives;
- our expected financings and investments;
- our regulatory structure and tax treatment;
- our ability to operate as a business development company and to be taxed as a regulated investment company;
- the adequacy of our cash resources and working capital; and
- the timing of cash flows, if any, from the operations of our portfolio companies.

The foregoing list is not exhaustive. In light of the foregoing, prospective investors are cautioned that the forward-looking statements included in this filing may ultimately prove to be inaccurate—even materially inaccurate. For a more complete summary of the risks and uncertainties facing our company and its business and relating to our forward-looking statements, please refer to our Annual Report on Form 10-K filed on March 31, 2015 (related to our year ended December 31, 2014) and in particular the section thereof entitled “Risk Factors.” Because of the significant uncertainties inherent in the forward-looking statements pertaining to our company, the inclusion of such information should not be regarded as a representation or warranty by us or any other person that our objectives, plans, expectations or projections that are contained in this filing will be achieved in any specified time frame, if ever. We undertake no obligation to update any forward-looking statement to reflect events or circumstances occurring after the date of this report. The forward-looking statements made in this report relate only to events as of the date on which the statements are made, and are excluded from the safe harbor protection provided by Section 21E of the Securities Exchange Act of 1934.

General Overview

Mill City Ventures III, Ltd. is a Minnesota corporation that was incorporated in January 2006. Until December 13, 2012, we were a development-stage company that previously focused on promoting and placing our Winner's Pot Poker game online and into casinos and entertainment facilities nationwide, including those located in Native American tribal lands. On December 13, 2012, we filed a Form N-8A with the SEC, notifying the SEC of our intent to register as an internally managed, non-diversified, closed-end investment company under the Investment Company Act of 1940 (the "1940 Act"). On February 7, 2013, we filed Form N-54A, Notification of Election to be Subject to Sections 55 through 65 of the 1940 Act, to be regulated as a business development company ("BDC"). Subsequently, on May 13, 2013, we filed Form N-8F to deregister as a registered investment company based upon our prior filing to become a BDC. On September 25, 2013, the SEC issued an order under Section 8(f) of the Investment Company Act of 1940 declaring that we had ceased to be an investment company. We are regulated as a BDC and we plan to be taxed as a regulated investment company ("RIC") although we have not made an election to be taxed as a RIC at this time.

Business Model and Strategy

As a BDC, we primarily focus on investing in, lending to and making managerial assistance available to privately held and publicly traded companies. A BDC may provide shareholders with the ability to retain the liquidity of a publicly traded stock, while sharing in the possible benefits of investing in emerging-growth or expansion-stage companies.

Our future revenues will relate to the earnings we receive from our portfolio investments. Our objective is to obtain superior returns from investments in securities and other investment opportunities available to BDC's under the 1940 Act. We intend to invest capital in portfolio companies for purposes of financing acquisitions, recapitalizations, buyouts, organic growth and working capital. Buyouts generally include transactions that involve the acquisition of a controlling interest in an entity, either by management or other investors. Organic growth refers to growth through the internal operations of the company, through investments in marketing initiatives, capital expenditures or other internal growth initiatives, rather than growth by means of an acquisition.

We plan to identify potential investments through multiple sources, including private equity sponsors, investment bankers, brokers, our Board of Directors, owners and operators of businesses and other persons within our professional network. We will base our investment decisions primarily on analyses of potential growth prospects of business operations and asset valuations. Subject to applicable BDC regulations set forth in the 1940 Act, we plan to invest in private companies, small-cap public stocks, notes and other forms of debt, investment contracts, and other investments commonly referred to as securities.

Highlights for the Three Months Ended March 31, 2015

Investment Transactions

On February 19, 2015, we purchased a 12% convertible note from Creative Realities, Inc. for $1,000,000 principal amount. The note bears 12% annual interest paid monthly in arrears and is due August 18, 2016. The outstanding principal amount is convertible into common stock at $0.33. In conjunction with the financing, we received a warrant to purchase 1,515,152 common shares with a conversion price of $0.38. The warrant has a cashless conversion provision and expires February 17, 2020.

On March 13, 2015, we purchased a 12% senior secured promissory note from Mix 1 Life, Inc. for $250,000 principal amount. At closing, 12 months of interest was prepaid by Mix 1. The note is due on March 13, 2016. Our director Christopher Larson is also a director and the Chief Financial Officer of Mix 1 Life as well as a 5% shareholder in Mix 1.

Material Changes in Assets and Liabilities

Our prepaid expenses as of March 31, 2015 were $25,414 compared to $49,623 for the year ended December 31, 2014. The decrease relates to our annual insurance and fidelity bond premiums. These premiums will be amortized ratably over the covered period.

Our accounts payable as of March 31, 2015 were $26,442 compared to $36,098 for the year ended December 31, 2014. The decrease relates to a reduction in accounting and other professional fees.

Our interest and dividends receivable at March 31, 2015 were $100,547 compared to $59,794 for the year ended December 31, 2014. The increase relates to our investments in Insite Software Solutions, Inc, DBR Phase III US Investors, LLC, The Igloo LLC, Mix 1 Life Inc., and Creative Realities Inc.

On August 7, 2014 we elected to exercise, on a cashless basis, our warrants of Mix 1 Life, Inc. into 1,121,912 shares of common stock. On September 11, 2014, a 1-for-3 reverse split on those common shares reduced our holdings to 373,971 common shares. At March 31, 2015, the cost and fair value of the warrant and common stock was $0 and $2,002,554, respectively.

Results of Operations for the Three Months Ended March 31, 2015 Compared to the Three Months Ended March 31, 2014

Operating Expenses

Item	**For the Three-Month Period Ended March 31, 2015**	**% of 2015 Net Income**	**For the Three-Month Period Ended March 31, 2014**	**% of 2014 Net Loss**
Investment Income	$ 163,844	271,715 %	41,764	(38.1)%
Operating Expenses:				
Professional fees	51,397	(85,235)%	37,177	33.9 %
Payroll expense	41,474	(68,779)%	41,446	37.9 %

Registration statement expense		-	-	%	-		-	%
Occupancy expense		22,799	(37,809	)%	17,406		15.9	%
Insurance expense		24,564	(40,736	)%	33,321		30.4	%
Directors' fees expense		15,000	(24,876	)%	15,000		13.7	%
Depreciation and amortization		3,212	(5,327	)%	3,098		2.8	%
Other general and administrative		4,795	(8,952	)%	3,850		3.5	%
Net Investment Gain (Loss)	$	603	100.0	%	(109,534	)	100.0	%

As the table above demonstrates, we incurred operating expenses of $163,241 and $151,298 for the three-month periods ended March 31, 2015 and 2014, respectively. A discussion and analysis of the material components of our operating expenses appears below.

Professional fees. Our professional fees were $51,397 for the three-month period ended March 31, 2015, compared to $37,177 for the three-month period ended March 31, 2014. The increase in professional fees is due to increased legal fees associated with the preparation of the Company's filing requirements.

Payroll expense and executive management compensation. During the three-month period ended March 31, 2015, we incurred $41,474 in payroll expense for our executive management compared to $41,446 incurred during the three-month period ended March 31, 2014.

Insurance expense. During the three-month period ended March 31, 2015, we incurred $24,564 in insurance expense compared to $33,321 for the three-month period ended March 31, 2014. Insurance expense relates to our annual director and officer insurance, fidelity bond premiums and business insurance amortized ratably over the covered period.

Directors' fees expense. Our directors' fees expense for the three-month periods ended March 31, 2015 and 2014 were $15,000.

We appointed independent members (qualifying as non-interested persons under the 1940 Act) to our Board of Directors and began compensating our directors as part of our transition to a BDC.

Occupancy expense. Our occupancy expenses for the three-month periods ended March 31, 2015 and 2014 were $22,799 and $17,406.

Net Investment Income (Loss)

Net investment income (loss) represents the difference between investment income and operating expenses. Our net investment income (loss) for the three-month period ended March 31, 2015 and 2014 was $603 and ($109,534), respectively. The increase was better results from investing activities and realization of profits on securities sold.

Net Realized Gains, Increase in Net Assets from Net Changes in Unrealized Appreciation

Net realized gains on investments for the three-month period ended March 31, 2015 was $146,853. A net realized gain of $164,728 was due to our sale of 27,667 shares of Mix 1 Life, Inc. common stock, and a $67,315 realized loss was due to our sale of 25,000 common shares of Bio Life Solutions, Inc.

The net increase in net assets from changes in unrealized appreciation was $5,723.

Liquidity and Capital Resources

Summary cash flow data is as follows:

	Three Months Ended March 31,	
	2015	2014
Cash flows used by :		
Operating activities	$ (1,322,674)	$ (719,353)
Investing activities	-	(6,504)
Financing activities	-	-
Net decrease in cash	(1,322,674)	(725,857)
Cash, beginning of period	4,105,911	7,090,379
Cash, end of period	$ 2,783,237	$ 6,364,522

The cash used in operating activities for the three-month period March 31, 2015 was primarily from our investment transactions.

On February 19, 2015, we purchased a 12% convertible note from Creative Realities, Inc. for $1,000,000 principal amount. The note bears 12% annual interest paid monthly in arrears and is due August 18, 2016. The outstanding principal amount is convertible into common stock at $0.33. In conjunction with the financing, we received a warrant to purchase 1,515,152 common shares with a conversion price of $0.38. The warrant has a cashless conversion provision and expires February 17, 2020.

On March 13, 2015, we purchased a 12% senior secured promissory note from Mix 1 Life, Inc. for $250,000 principal amount. At closing, 12 months of interest was prepaid by Mix 1. The note is due on March 13, 2016. Our director

Christopher Larson is also a director and the Chief Financial Officer of Mix 1 Life as well as a 5% shareholder in Mix 1.

Regulation as a BDC

As a BDC, we are regulated by the 1940 Act. A BDC must be organized in the United States for the purpose of investing in or lending to primarily private companies, or certain small-cap public companies, and, with limited exceptions, making managerial assistance available to them. A BDC may use capital provided by public shareholders and from other sources to make long-term, private investments in businesses. A BDC may provide shareholders the ability to retain the liquidity of a publicly traded stock while sharing in the possible benefits, if any, of investing in primarily privately owned or small-cap public companies.

We may not change the nature of our business so as to cease to be, or withdraw our election as, a BDC unless authorized by vote of a majority of the outstanding voting securities, as required by the 1940 Act. A majority of the outstanding voting securities of a company is defined under the 1940 Act as the lesser of: (a) 67% or more of such company's voting securities present at a meeting if more than 50% of the outstanding voting securities of such company are present or represented by proxy; or (b) more than 50% of the outstanding voting securities of such company. We do not anticipate any substantial change in the nature of our business.

As with other companies regulated by the 1940 Act, a BDC must adhere to certain substantive regulatory requirements. A majority of our directors must be persons who are not "interested persons," as that term is defined in the 1940 Act. Additionally, we are required to provide and maintain a bond issued by a reputable fidelity insurance company to protect the BDC. Furthermore, as a BDC, we are prohibited from protecting any director or officer against any liability to us or our shareholders arising from willful misfeasance, bad faith, gross negligence or reckless disregard of the duties involved in the conduct of such person's office.

We are generally not able to sell our common stock at a price below net asset value per share. We may, however, sell our common stock at a price below net asset value per share (i) in connection with a rights offering to our existing shareholders, (ii) with the consent of shareholders holding a majority of our common stock, or (iii) under such other circumstances as the SEC may permit. For example, we may sell our common stock at a price below the then-current net asset value of our common stock if our Board of Directors determines that such sale is in our best interests and the best interests of our shareholders, and our shareholders approve our policy and practice of making such sales. In addition, we may generally issue new shares of our common stock at a price below net asset value in rights offerings to our existing shareholders, in payment of dividends and in certain other limited circumstances. No such offerings have occurred as of the date of this filing.

We will be permitted, under specified conditions, to issue multiple classes of indebtedness and one class of stock senior to our common stock, but only if our “asset coverage,” as defined in the 1940 Act, is at least equal to 200% immediately after each such issuance. In addition, while any senior securities remain outstanding, we must not make any dividend distribution to our shareholders or repurchase securities unless we meet the applicable asset-coverage ratios at the time of the dividend distribution or repurchase. We may also borrow amounts up to 5% of the value of our total assets for temporary or emergency purposes.

We are prohibited under the 1940 Act from knowingly participating in certain transactions with our affiliates without the prior approval of our directors who are not interested persons and, in some cases, prior approval by the SEC. Subject to certain exceptions, as a BDC, we are generally not permitted to invest in any portfolio company in which our affiliates currently have an investment or to make any co-investments with our affiliates without an exemptive order from the SEC.

We will be periodically examined by the SEC for compliance with the 1940 Act, the rules and regulations thereunder, and good governance practices. We will not “concentrate” our investments (i.e., invest 25% or more of our assets in any particular industry, determined at the time of investment). We will be required to provide and maintain a bond issued by a reputable fidelity insurance company to protect us against larceny and embezzlement. Furthermore, as a BDC, we are prohibited from indemnifying any director or officer against any liability to our shareholders arising from willful malfeasance, bad faith, gross negligence or reckless disregard of the duties involved in the conduct of such person’s office. We are required to adopt and implement written policies and procedures reasonably designed to prevent violation of the federal securities laws, review these policies and procedures annually for their adequacy and the effectiveness of their implementation.

Qualifying Assets

Under the 1940 Act, a BDC may not acquire any asset other than “qualifying assets” listed in Section 55(a) of the 1940 Act unless, at the time the acquisition is made, qualifying assets represent at least 70% of the BDC’s total assets. The principal categories of qualifying assets relevant to our business are the following:

(1) Securities of an "eligible portfolio company" purchased from the issuer of such securities or from a person who is, or who was within the prior 13 months of the date of purchase, an affiliate of the issuer or from any other person (subject to limitation by SEC rules), in any case in transactions not involving any public offering. The 1940 Act defines an "eligible portfolio company" as any issuer which:

(a) is organized under the laws of, and has its principal place of business in, the United States;

(b) is not an investment company or a company that would be an investment company but for certain exclusions under the 1940 Act; and

(c) satisfies one of the following:

(i) does not have outstanding any class of securities with respect to which a broker or dealer may extend margin credit (or, if a broker or dealer may in fact extend or maintain margin credit to a customer with respect to such securities, then at the time of purchase of the issuer's securities (A) the BDC owns at least 50% of the greatest number of outstanding and issuable equity securities of such issuer (i.e., 50% determined on a fully diluted basis) and the greatest amount of debt securities of such issuer), (B) the BDC is one of the 20 largest holders of record of the issuer's outstanding voting securities);

(ii) is controlled by a BDC or a group of companies acting together that includes a BDC, the BDC does in fact exercise a controlling influence over the management or policies of the issuer, and, as a result of such control, the BDC has an affiliated person serving as a director of the eligible portfolio company;

(iii) is a small and solvent company having total assets of not more than $4 million and capital and surplus of not less than $2 million, subject to adjustment by SEC rules; or

(iv) by virtue of SEC Rule 2a-46, (A) does not have any class of securities listed on a national securities exchange, or (B) has a class of securities listed on a national securities exchange but an aggregate market value (as computed under such rule) of outstanding voting and non-voting common equity of less than $250 million.

(2) Securities of any eligible portfolio company (as defined above) that we control through having a person serving on the board of directors of the issuer.

(3) Securities purchased from an issuer, or from a person who is, or was in the prior 13 months of the date of purchase, an affiliate of the issuer, which issuer is organized under the laws of, and has its principal place of business in, the United States and is not an investment company (or a company that would be an investment company but for certain exclusions under the 1940 Act), and which is in bankruptcy and subject to reorganization (or where the issuance of securities is consummated pursuant to or in consummation of a bankruptcy or reorganization plan or arrangement).

(4) Securities of an eligible portfolio company (as defined above) purchase from any person in a transaction not involving a public offering, if there is no ready market for such securities and if immediately prior to such purchase the BDC owns at least 60% of the outstanding equity securities of such issuer, as determined on a fully diluted basis.

(5) Securities received in exchange for or distributed on or with respect to securities described above, or pursuant to the conversion of warrants or rights relating to such securities.

(6) Cash, cash equivalents, U.S. government securities or high-quality debt securities maturing in one year or less from the time of investment.

(7) Office furniture and equipment, interests in real estate and leasehold improvement and facilities maintained to conduct the business operations of the BDC, deferred organization and operating expenses, and other non-investment assets necessary and appropriate to its operations as a BDC, including notes of indebtedness of directors, officers, employees and general partners held by the BDC as payment for securities of such company issued in connection with an executive compensation plan described in Section 57(j) of the 1940 Act.

In addition to the foregoing description of “qualifying assets,” certain types of follow-on investments in issuers that no longer satisfy the definition of “eligible portfolio company” may nonetheless be “qualifying assets.”

Significant Managerial Assistance or Control

A BDC must have been organized and have its principal place of business in the United States and must be operated for the purpose of making investments in the types of securities described above. Nevertheless, to count portfolio securities as qualifying assets for the purpose of the foregoing 70% test, the BDC must either control the issuer of the securities or offer to make available to the issuer of the securities (other than small and solvent companies described above) significant managerial assistance; except that, where the BDC purchases such securities in conjunction with one or more other persons acting together, one of the other persons in the group may make available such managerial assistance. Making available significant managerial assistance means, among other things, any arrangement whereby the BDC, whether through its directors, officers or employees, offers to provide, and, if accepted, does in fact so provide, significant guidance and counsel concerning the management, operations or business objectives and policies of a portfolio company through monitoring of portfolio company operations, selective participation in board and management meetings, consulting with and advising a portfolio company's officers or other organizational or financial guidance.

Temporary Investments

Pending investment in other types of qualifying assets, as described above, our investments may consist of cash, cash equivalents, U.S. government securities or high quality debt securities maturing in one year or less from the time of investment, which we refer to, collectively, as temporary investments, so that at least 70% of our assets are qualifying assets. We plan to invest in U.S. treasury bills or in repurchase agreements, provided that such agreements are fully collateralized by cash or securities issued by the U.S. government or its agencies. A repurchase agreement involves the purchase by an investor, such as us, of a specified security and the simultaneous agreement by the seller to repurchase it at an agreed upon future date and at a price which is greater than the purchase price by an amount that reflects an agreed-upon interest rate. There is no percentage restriction on the proportion of our assets that may be invested in such repurchase agreements. However, if more than 25% of our total assets constitute repurchase agreements from a single counterparty, we would not meet the diversification tests imposed on us by the Internal Revenue Code to qualify for tax treatment as a RIC for federal income tax purposes. Thus, we do not intend to enter into repurchase agreements with a single counterparty in excess of this limit. We will monitor the creditworthiness of the counterparties with which we enter into repurchase agreement transactions.

Capital Expenditures

We did not have and do not plan to have any material commitments for capital expenditures in 2014 or 2015. Given our business model and status as a BDC, we do not require material investments in capital resources.

Certain Potential Conflicts of Interest

Our Company maintains a Code of Ethics and certain other policies relating to conflicts of interest and related-party transactions, as well as policies and procedures relating to what applicable BDC regulations generally describe as “affiliate transaction.” Nevertheless, from time to time we may hold investments in portfolio companies in which certain members of our management are also directly or indirectly invested. Our Board of Directors has recently adopted a policy to require our disclosure of these instances in our periodic filings with the SEC. Presently, each of Messrs. Geraci and Polinsky have direct and indirect interests in Southern Plains Resources, Inc. We invested in Southern Plains Resources in each of March and July 2013. In addition, our director Christopher Larson has a direct interest in Mix 1 Life, Inc. and served as that company’s Chief Financial Officer at the time of our investment. We invested in Mix 1 Life in February 2014 and we exercised, on a cashless basis, a warrant for the purchase of Mix 1 Life common stock in September 2014. Subsequent to our initial investment, Mr. Larson became a director of Mix 1 Life.

Critical Accounting Policies

Investment Valuation

Investment transactions are recorded on the trade date. Realized gains or losses are measured by the difference between the net proceeds from the repayment or sale and the amortized cost basis of the investment without regard to unrealized gains or losses previously recognized, and include investments charged off during the period, net of recoveries. Unrealized gains or losses primarily reflect the change in investment values, including the reversal of previously recorded unrealized gains or losses when gains or losses are realized.

Investments for which market quotations are readily available are typically valued at such market quotations. In order to validate market quotations, we look at a number of factors to determine if the quotations are representative of fair value, including the source and nature of the quotations. Debt and equity securities that are not publicly traded or whose market prices are not readily available are valued at fair value as determined in good faith by our board of directors, based on, among other things, the input of our executive management, audit committee and independent third-party valuation expert that may be engaged by management to assist in the valuation of our portfolio investments.

Realized Gains and Losses, Interest and Dividend Income Recognition

Realized gains or losses on the sale of investments are calculated using the specific investment method.

Interest income is recorded on an accrual basis and includes the accretion of discounts and amortization of premiums. Discounts from and premiums to par value on securities purchased are accreted/amortized into interest income over the life of the respective security using the effective yield method. The amortized cost of investments represents the original cost adjusted for the accretion of discounts and amortization of premiums, if any.

Loans are generally placed on non-accrual status when principal or interest payments are past due 30 days or more or when there is reasonable doubt that principal or interest will be collected in full. Accrued and unpaid interest is generally reversed when a loan is placed on non-accrual status. Interest payments received on non-accrual loans may be recognized as income or applied to principal depending upon management’s judgment regarding collectability. Non-accrual loans are restored to accrual status when past due principal and interest is paid and, in management’s judgment, are likely to remain current. We may make exceptions to this if the loan has sufficient collateral value and is in the process of collection.

Dividend income on preferred equity securities is recorded as dividend income on an accrual basis to the extent that such amounts are payable by the portfolio company and are expected to be collected. Dividend income on common equity securities is recorded on the record date for private portfolio companies or on the ex-dividend date for publicly traded portfolio companies.

Further information on our critical accounting policies and use of estimates can be found in our financial statements and notes thereto included in this report and in our Annual Report on Form 10-K filed with the SEC on March 31, 2014. There have been no material changes to our critical accounting policies and estimates from those disclosed in our Annual Report on Form 10-K.

Off-Balance Sheet Arrangements

During the three months ended March 31, 2015, we did not engage in any off-balance sheet arrangements set forth in Item 303(a)(4) of Regulation S-K.

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Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures designed to provide reasonable assurance that information required to be disclosed in our reports filed pursuant to the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer as appropriate, to allow timely decisions regarding required disclosure. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance the objectives of the control system are met.

As of March 31, 2015, our Chief Executive Officer and Chief Financial Officer carried out an evaluation of the effectiveness of our disclosure controls and procedures as such term is defined in Rule 13a-15(e) under the Securities and Exchange Act of 1934. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded our disclosure controls and procedures are effective as of March 31, 2015.

Changes in Internal Controls

There were no significant changes in our internal controls over financial reporting that occurred during the fiscal quarter covered by this report that materially affected, or were reasonably likely to materially affect such controls.

PART II – OTHER INFORMATION

Item 6. Exhibits

Exhibit No.	Description
31.1	Certification of Chief Executive Officer (filed herewith).
31.2	Certification of Chief Financial Officer (filed herewith).
32	Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed herewith).

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SIGNATURES

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

MILL CITY VENTURES III, LTD.

/s/ Douglas Polinsky
Douglas Polinsky
Chief Executive Officer

Dated: May 12, 2015

/s/ Joseph A. Geraci, II
Joseph A. Geraci, II
Chief Financial Officer

Dated: May 12, 2015