Mill City Ventures III, Ltd
Form 10-Q
May 14, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 2018

or

.. TRANSITION REPORT PURSUANT TO 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, Minnesota	**55391**
(Address of principal executive offices)	(Zip Code)

(952) 479-1923

(Registrant’s telephone number, including area code)

N/A

(Former name, former address and former fiscal year, if changed since 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. x Yes ¨ No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, 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). x Yes ¨ No

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

Large accelerated filer ¨	Accelerated filer ¨
Non-accelerated filer ¨	Smaller reporting company x
	Emerging growth company ¨

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ¨

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

As of May 11, 2018, Mill City Ventures III, Ltd. had 11,067,402 shares of common stock, and no other classes of capital stock, outstanding.

MILL CITY VENTURES III, LTD.

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for the Quarter Ended March 31, 2018

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

MILL CITY VENTURES III, LTD.

BALANCE SHEETS

	March 31, 2018 (unaudited)	December 31, 2017 (audited)
ASSETS		
Investments, at fair value:	$ 8,482,227	$ 7,240,860
Non-control/non-affiliate investments (cost: $7,602,218 and $7,000,745 respectively)		
Cash	1,765,268	2,158,314
Prepaid expenses	35,357	62,549
Receivable for sale of investments	—	267,119
Interest and dividend receivables	45,060	39,574
Leasehold improvements, net	5,529	7,557
Property and equipment, net	6,575	7,218
Total Assets	$ 10,340,016	$ 9,783,191
LIABILITIES		
Current Liabilities		
Accounts payable	$ 40,307	$ 37,091
Payable for purchase of investments	120,637	106,222
Deferred rent	10,267	10,663
Total Current Liabilities	171,211	153,976
Total Liabilities	171,211	153,976
Commitments and Contingencies (Note 6)		
SHAREHOLDERS EQUITY (NET ASSETS)		
Common Stock, par value $0.001 per share (250,000,000 authorized; 11,067,402 and 11,067,402 outstanding)	11,067	11,067
Additional paid-in capital	10,774,653	10,774,653
Accumulated deficit	(1,159,665)	(1,159,665)
Accumulated undistributed investment loss	(1,346,829)	(1,194,773)
Accumulated undistributed net realized gains on investment transactions	1,009,570	957,818
Net unrealized appreciation in value of investments	880,009	240,115
Total Shareholders' Equity (net assets)	10,168,805	9,629,215

Total Liabilities and Shareholders' Equity	$ 10,340,016	$ 9,783,191
Net Asset Value Per Common Share	$ 0.92	$ 0.87

See accompanying Notes to Financial Statements

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MILL CITY VENTURES III, LTD.

STATEMENTS OF OPERATIONS (UNAUDITED)

	Three Months Ended	
	March 31, 2018	March 31, 2017
Investment Income		
Interest income	$34,146	$ 23,197
Dividend income	379	13,367
Total Investment Income	34,525	36,564
Operating Expenses		
Professional fees	60,281	66,736
Payroll	61,053	41,358
Insurance	18,891	17,446
Occupancy	22,755	19,822
Director's fees	15,000	15,000
Depreciation and amortization	2,671	2,748
Other general and administrative	5,930	3,104
Total Operating Expenses	186,581	166,214
Net Investment Loss	$(152,056)	$ (129,650)
Realized and Unrealized Gain (Loss) on Investments		
Net realized gain on investments	51,752	712,271
Net change in unrealized appreciation (depreciation) on investments	639,894	(603,139)
Net Realized and Unrealized Gain on Investments	691,646	109,132
Net Increase (Decrease) in Net Assets Resulting from Operations	$539,590	$ (20,518)
Net Increase (Decrease) in Net Assets Resulting from Operations per share:		
Basic and diluted	$0.05	$ 0.00
Weighted-average number of common shares outstanding	11,067,402	12,151,493

See accompanying Notes to Financial Statements

MILL CITY VENTURES III, LTD.

STATEMENTS OF CHANGES IN NET ASSETS (UNAUDITED)

	Three Months Ended March 31, 2018	Three Months Ended March 31, 2017
Net Assets at Beginning of Period	$ 9,629,215	$ 9,387,408
Net investment loss	(152,056)	(129,650)
Net realized gain on investments	51,752	712,271
Net increase (decrease) in unrealized appreciation on investments	639,894	(603,139)
Net increase (decrease) in net assets resulting from operations	539,590	(20,518)
Total net increase (decrease) in net assets resulting from operations	539,590	(20,518)
Net Assets at End of Period	$ 10,168,805	$ 9,366,890
Accumulated undistributed net investment loss	$ (1,346,829)	$ (1,459,855)

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MILL CITY VENTURES III, LTD.

STATEMENTS OF CASH FLOWS (UNAUDITED)

	Three Months Ended	
	March 31, 2018	March 31, 2017
Cash flows from operating activities:		
Net increase (decrease) in net assets resulting from operations	$539,590	$ (20,518)
Adjustments to reconcile net increase (decrease) in net assets resulting from operations to net cash (used) provided in operating activities:		
Net change in unrealized (appreciation) depreciation on investments	(639,894)	603,139
Net realized gain on investments	(51,752)	(712,271)
Payments for purchases of investments	(628,252)	(694,120)
Proceeds from sales of investments	78,531	2,321,114
Depreciation and amortization expense	2,671	2,748
Changes in operating assets and liabilities:		
Prepaid expenses	27,192	22,441
Interest and dividends receivable	(5,486)	(5,895)
Receivable for sales of investments	267,119	(2,057)
Accounts payable	3,216	5,993
Payable for purchase of investments	14,415	205,698
Deferred rent	(396)	(157)
Net cash (used) provided in operating activities	(393,046)	1,726,115
Net (decrease) increase in cash	(393,046)	1,726,115
Cash, beginning of period	2,158,314	2,344,751
Cash, end of period	$1,765,268	$ 4,070,866

See accompanying Notes to Financial Statements

MILL CITY VENTURES III, LTD.

SCHEDULE OF INVESTMENTS

MARCH 31, 2018

Investments [1]	Investment Type	**Interest Rate** [2]	Maturity Date	Principal Amount	Cost	Fair Value	Percentage of Net Assets	Gross Unrealized Appreciation	Gross Unrealized Depreciation	Net Unrealized Appreciation (Depreciation
Debt Investments										
Consumer										
Mix 1 Life, Inc.	Secured Loan [3]	12%	2/6/2016	$500,000	$500,000	$—		$—	$500,000	$(500,000)
Mix 1 Life, Inc.	Secured Loan	12%	3/13/2016	$250,000	250,000	—		—	250,000	(250,000)
					750,000	—	0.00%	—	750,000	(750,000)
Financial										
Bravo Financial LLC	Secured Loan	12%	8/31/2018	$500,000	500,000	500,000	4.92%	—	—	—
Total Debt Investments					$1,250,000	$500,000	4.92%	$—	$750,000	$(750,000)

Investments [1]	**Investment Type** [4]	**Interest Rate** [5]	**Expiration Date** [6]	Shares/Units	Cost	Fair Value	Percentage of Net Assets	Gross Unrealized Appreciation	Gross Unrealize Deprecia
Equity Investments									
Advertising									
Creative Realities, Inc.	Warrants [7]	n/a	12/28/2020	1,071,429	$—	$21,429	0.21%	$21,429	$—
Business Services									
Spar Group Inc.	Common Stock [7]	n/a	n/a	159,406	227,728	223,168	2.19%	3,261	7,821
Consumer									
Bridgford Foods Company	Common Stock	n/a	n/a	2,959	43,805	44,267		609	147
Famous Daves of America, Inc.	Common Stock	n/a	n/a	37,923	159,087	269,253		110,166	—
HG Holdings, Inc.	Common Stock [7]	n/a	n/a	200,000	199,118	120,000		—	79,118

Mix 1 Life, Inc.	Common Stock	n/a	n/a	100,000	46,160	—		—	46,160
Tzfat Spirits of Israel, LLC	LLC Membership Units (7)	n/a	n/a	55,000	101,019	25,000		—	76,019
					549,189	458,520	4.51 %	110,775	201,444
Education									
Nat'l Amer. Univ. Holdings, Inc.	Common Stock	n/a	n/a	114,753	186,693	149,844	1.47 %	5,406	42,255
Financial									
OTC Markets Group Cl A	Common Stock	n/a	n/a	11,226	181,748	300,857		119,109	—
Hi-Crush Partners, LP	Common Stock (8)	n/a	n/a	10,000	104,222	106,000		1,778	—
QC Holdings, Inc.	Common Stock (7)	n/a	n/a	15,000	10,655	8,100		—	2,555
					296,625	414,957	4.08 %	120,887	2,555

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Healthcare									
Reshape Life Sciences Inc Pfd Conv Ser B	Preferred LLC Units [3] [7]	n/a	n/a	156	155,321	98,397		—	56,924
Reshape Life Sciences Inc Pfd Conv Ser B	Warrants [7]	n/a	8/16/2024	67,860	679	—		—	679
HemaCare Corp.	Common Stock [7]	n/a	n/a	139,697	430,877	810,243		379,366	—
Opiant Pharmaceuticals, Inc.	Common Stock [7]	n/a	n/a	5,000	104,133	95,900		299	8,532
					691,010	1,004,540	9.88 %	379,665	66,135
Industrial Goods									
ClearSign Combustion Corporation	Common Stock	n/a	n/a	3,400	11,310	6,885	0.07 %	—	4,425
Information Technology									
Insite Software Solutions, Inc	Warrants [7]	n/a	12/30/2023	108,960	—	—		—	—
MAX 4G, Inc.	Preferred Stock [7]	n/a	n/a	300,000	150,000	300,000		150,000	—
Simulations Plus, Inc.	Common Stock	n/a	n/a	25,001	246,710	368,758		122,048	—
Travelzoo, Inc.	Common Stock	n/a	n/a	34,150	354,633	248,441		426	106,618
					751,343	917,199	9.02 %	272,474	106,618
Leisure & Hospitality									
Bitesquad.com LLC	Preferred LLC Units [3] [7]	n/a	n/a	73,543	1,014,893	2,020,226		1,005,333	—
DBR Enclave US Investors, LLC	LLC Membership Units	15 %	1/31/2020	500,000	500,000	500,000		—	—
					1,514,893	2,520,226	24.78 %	1,005,333	—
Oil & Gas									
Matrix Service Company	Common Stock [7]	n/a	n/a	10,000	182,580	137,000		—	45,580
Northern Capital Partners I, LP	Limited Partnership Units [7]	n/a	n/a	550,000	550,000	488,629		—	61,371
Southern Plains Resources, Inc.	Common Stock [7]	n/a	n/a	600,000	730,000	—		—	730,000
					1,462,580	625,629	6.15 %	—	836,951
Publishing									

Educational Development Corp.	Common Stock	n/a	n/a	65,202	660,847	1,639,830	16.13 %	978,983	—
Total Equity Investments					$6,352,218	$7,982,227	78.49 %	$2,898,213	$1,268,20
Total Investments					7,602,218	8,482,227	83.41 %	2,898,213	2,018,20
Total Cash					1,765,268	1,765,268	17.36 %	—	—
Total Investments and Cash					$9,367,486	$10,247,495	100.77%	$2,898,213	$2,018,20

(1) All investments and all cash are “qualifying assets” under Section 55(a) of the Investment Company Act of 1940 unless indicated to the contrary in the table or by footnote.
(2) Interest is presented on a per annum basis.
(3) Investment is convertible into common equity of the issuer.
(4) In the case of warrants, warrants provide for the right to purchase common equity of the issuer.
(5) In the case of preferred stock, this represents the right to annual cumulative dividends calculated on a per annum basis.
(6) In the case of warrants, purchase rights under the warrants will expire at the close of business on this date.
(7) Investment is not an income-producing investment.
(8) Investment is neither a “qualifying asset” under Section 55(a) of the Investment Company Act of 1940, nor a restricted security.

At March 31, 2018, aggregate non-qualifying assets represented approximately 1.2% of our total assets.

At March 31, 2018, the estimated net unrealized gain for federal tax purposes was $1,078,681, based on a tax cost basis of $7,403,546.

At March 31, 2018, the estimated aggregate gross unrealized gain for federal income tax purposes was $2,984,953 and the estimated aggregate gross unrealized loss for federal income tax purposes was $1,906,272

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MILL CITY VENTURES III, LTD.

SCHEDULE OF INVESTMENTS

DECEMBER 31, 2017

Investments [1]	Investment Type	**Interest Rate** [2]	Maturity Date	Principal Amount	Cost	Fair Value	Percentage of Net Assets	Gross Unrealized Appreciation	Gross Unrealized Depreciation	Net Unrealize Apprecia (Deprecia
Debt Investments										
Consumer										
Mix 1 Life, Inc.	Secured Loan [3]	12%	2/6/2016	$500,000	$500,000	$—		$—	$500,000	$(500,00
Mix 1 Life, Inc.	Secured Loan	12%	3/13/2016	$250,000	250,000	—		—	250,000	(250,00
					750,000	—	0.00%	—	750,000	(750,00
Financial										
Bravo Financial LLC	Secured Loan	12%	8/31/2018	$500,000	500,000	500,000	5.19%	—	—	—
Total Debt Investments					$1,250,000	$500,000	5.19%	$—	$750,000	$(750,00

Investments [1]	**Investment Type** [4]	**Interest Rate** [5]	**Expiration Date** [6]	Shares/Units	Cost	Fair Value	Percentage of Net Assets	Gross Unrealized Appreciation	Gross Unrealized Depreciati
Equity Investments									
Advertising									
Creative Realities, Inc.	Warrants [7]	n/a	12/28/2020	1,071,429	$—	$42,857	0.45%	$42,857	$—
Consumer									
Famous Daves of America, Inc.	Common Stock	n/a	n/a	37,923	159,087	248,395		89,308	—
Forward Industries, Inc.	Common Stock [7]	n/a	n/a	20,100	23,969	24,723		778	24
Mix 1 Life, Inc.	Common Stock [9]	n/a	n/a	100,000	46,160	800		—	45,360
Stanley Furniture Co., Inc.	Common Stock [7]	n/a	n/a	171,292	181,871	149,024		—	32,847
Tzfat Spirits of Israel, LLC	LLC Membership Units [7]	n/a	n/a	55,000	101,019	25,000		—	76,019

512,106	447,942	4.65%	90,086	154,250

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Education										
Nat'l Amer. Univ. Holdings, Inc.	Common Stock	n/a	n/a	100,000	172,757	142,000	1.47 %	3,321	34,078	(3
Financial										
OTC Markets Group Cl A	Common Stock	n/a	n/a	11,279	182,557	327,655		145,098	—	1
Hi-Crush Partners, LP	Common Stock (8)	n/a	n/a	10,000	106,222	107,000		778	—	7
QC Holdings, Inc.	Common Stock (7)	n/a	n/a	15,000	10,655	6,862		—	3,793	(3
					299,434	441,517	4.59 %	145,876	3,793	1
Healthcare										
Reshape Life Sciences Inc Pfd Conv Ser B	Preferred LLC Units (3) (7)	n/a	n/a	156	155,321	100,433		—	54,888	(5
Reshape Life Sciences Inc Pfd Conv Ser B	Warrants (7)	n/a	8/16/2024	67,860	679	—		—	679	(6
HemaCare Corp.	Common Stock (7)	n/a	n/a	136,897	421,839	413,429		6,396	14,806	(8
					577,839	513,862	5.34 %	6,396	70,373	(6
Industrial Goods										
ClearSign Combustion Corporation	Common Stock	n/a	n/a	3,400	11,310	12,240	0.12 %	930	—	9
Information Technology										
Insite Software Solutions, Inc	Warrants (7)	n/a	12/30/2023	108,960	—	—		—	—	—
MAX 4G, Inc.	Preferred Stock (7)	n/a	n/a	300,000	150,000	300,000		150,000	—	1
Simulations Plus, Inc.	Common Stock	n/a	n/a	25,001	246,710	402,509		155,799	—	1
Travelzoo, Inc.	Common Stock	n/a	n/a	30,000	324,848	193,500		—	131,348	(1
					721,558	896,009	9.31 %	305,799	131,348	1
Leisure & Hospitality										
Bitesquad.com LLC	Preferred LLC Units (3) (7)	n/a	n/a	73,543	1,014,893	2,020,226		1,005,333	—	1
		15 %	1/31/2020	500,000	500,000	500,000		—	—	—

DBR Enclave US Investors, LLC	LLC Membership Units									
					1,514,893	2,520,226	26.17%	1,005,333	—	1
Oil & Gas										
Northern Capital Partners I, LP	Limited Partnership Units (7)	n/a	n/a	550,000	550,000	488,629		—	61,371	(6
Southern Plains Resources, Inc.	Common Stock (7)	n/a	n/a	600,000	730,000	—		—	730,000	(7
					1,280,000	488,629	5.07 %	—	791,371	(7
Publishing Educational Development Corp.	Common Stock	n/a	n/a	65,202	660,848	1,235,578	12.83%	574,730	—	5
Total Equity Investments					$5,750,745	$6,740,860	70.00%	$2,175,328	$1,185,213	$9
Total Investments					7,000,745	7,240,860	75.19%	2,175,328	1,935,213	2
Total Cash					2,158,314	2,158,314	22.41%	—	—	—
Total Investments, and Cash					$9,159,059	$9,399,174	97.60%	$2,175,328	$1,935,213	$2

(1) All investments and all cash are "qualifying assets" under Section 55(a) of the Investment Company Act of 1940 unless indicated to the contrary in the table or by footnote.
(2) Interest is presented on a per annum basis.
(3) Investment is convertible into common equity of the issuer.
(4) In the case of warrants, warrants provide for the right to purchase common equity of the issuer.
(5) In the case of preferred stock, this represents the right to annual cumulative dividends calculated on a per annum basis.
(6) In the case of warrants, purchase rights under the warrants will expire at the close of business on this date.
(7) Investment is not an income-producing investment.
(8) Investment is neither a "qualifying asset" under Section 55(a) of the Investment Company Act of 1940, nor a restricted security.
At December 31, 2017, aggregate non-qualifying assets represented approximately 1.1% of our total assets.

(9) Value reflects 20% discount for restricted nature of securities
At December 31, 2017, the estimated net unrealized gain for federal tax purposes was $541,796, based on a tax cost basis of $6,699,064.

At December 31, 2017, the estimated aggregate gross unrealized gain for federal income tax purposes was $2,365,077, and the estimated aggregate gross unrealized loss for federal income tax purposes was $1,823,281

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MILL CITY VENTURES III, LTD.

NOTES TO FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2018

NOTE 1 – ORGANIZATION

Mill City Ventures III, Ltd. is an investment company incorporated in the State of Minnesota on January 10, 2006. In this report, we generally refer to Mill City Ventures III, Ltd. in the first person "we." On occasion, we refer to our company in the third person as "Mill City Ventures" or the "company." The company follows accounting and reporting guidance in Accounting Standards ("ASC") 946.

We are an internally managed closed-end non-diversified management investment company. We have elected to be regulated as a business development company, or "BDC," under the Investment Company Act of 1940 (the "1940 Act"). To date, we have not made an election to be treated as a regulated investment company, or "RIC," under the Internal Revenue Code of 1986 (the "Code").

We primarily focus on investing in or lending to privately held and small-cap publicly traded U.S. companies, and making managerial assistance available to such companies. These investments are typically structured as purchases of preferred or common stock, investment contracts, or loans evidenced by promissory notes that may be convertible into stock by their terms or that may be accompanied by the issuance to us of warrants or similar rights to purchase stock. Our investments may be made for purposes of financing acquisitions, recapitalizations, buyouts, organic growth and working capital. Our future revenues will relate to the gain we realize from the sale of securities we purchase, and to dividends and interest we derive from those securities. Our investment objective is to generate both current income and capital appreciation that ultimately result in gains.

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation: The accompanying unaudited condensed financial statements of Mill City Ventures have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-Q and Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States (GAAP) for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included. Operating results for the quarter ended March 31, 2018 are not necessarily indicative of the results that may be expected for the year ending December 31, 2018.

The condensed balance sheet as of December 31, 2017 has been derived from the audited consolidated financial statements at that date but does not include all of the information and footnotes required by GAAP for complete financial statements. For further information, refer to the financial statements and footnotes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2017.

Use of estimates: The preparation of financial statements in conformity with GAAP 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, as well as the reported amounts of expenses during the reporting period. Actual results could differ from those estimates. For more information, see the "Valuation of portfolio investments" caption below, and "Note 4 – Fair Value of Financial Instruments" below.

Cash deposits: We maintain our 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.

Valuation of portfolio investments: We carry our investments in accordance with ASC Topic 820, *Fair Value Measurements and Disclosures* ("ASC 820"), issued by the Financial Accounting Standards Board ("FASB"), which defines fair value, establishes a framework for measuring fair value, and requires disclosures about fair value measurements. Fair value is generally based on quoted market prices provided by independent pricing services, broker or dealer quotations, or alternative price sources. In the absence of quoted market prices, broker or dealer quotations, or alternative price sources, investments are measured at fair value as determined by the Valuation Committee of our Board of Directors based on, among other things, the input of our executive management, the Audit Committee of our Board of Directors, and any independent third-party valuation experts 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 uncertainties of valuation, certain estimated fair values may differ significantly from the values that would have been realized had a ready market for these investments existed, and these differences could be material. In addition, 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.

MILL CITY VENTURES III, LTD.

NOTES TO FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2018

For more information, see Note 4 “Fair Value of Financial Instruments.”

Income taxes: We account 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. For more information, see Note 7 “Income Taxes.”

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

Interest income, adjusted for amortization of premiums and accretion of discounts, is recorded on an accrual basis. Discounts from and premiums to par value on securities purchased are accreted or amortized, as applicable, into interest income over the life of the related 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 the policy described above if a 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.

Certain investments may have contractual payment-in-kind ("PIK") interest or dividends. PIK represents accrued interested or accumulated dividends that are added to the loan principal or stated value of the investment on the respective interest- or dividend-payment dates rather than being paid in cash, and generally becomes due at maturity or upon being repurchased by the issuer. PIK interest or dividends is recorded as interest or dividend income, as applicable. If at any point we believe that PIK interest or dividends is not expected be realized, the PIK-generating investment will be placed on non-accrual status. Accrued PIK interest or dividends are generally reversed through interest or dividend income, respectively, when an investment is placed on non-accrual status.

Recent accounting pronouncements: In February 2016, the Financial Accounting Standards Board issued Accounting Standards Update ("ASU") No. 2016-02, *Leases (Topic 842)*. The guidance in this ASU supersedes the leasing guidance in *Leases (Topic 840)*. Under the new guidance, lessees are required to recognize lease assets and lease liabilities on the balance sheet for those leases previously classified as operating leases. The guidance requires the use of a modified retrospective transition approach, which includes a number of optional practical expedients that entities may elect to apply. The amendments in ASU No. 2016-02 are effective for annual reporting periods beginning after December 15, 2018, including interim periods within that reporting period, with early adoption permitted. While we are currently evaluating the impact of ASU No. 2016-02, we expect an increase to the consolidated balance sheets for the lease assets and associated lease liabilities for our lease agreements previously accounted for as operating leases.

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.

Management and service fees: We do not incur expenses related to management and service fees. Our executive management team manages our investments as part of their employment responsibilities.

MILL CITY VENTURES III, LTD.

NOTES TO FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2018

NOTE 3 – INVESTMENTS

The following table shows the composition of our investment portfolio by major class, at amortized cost and fair value, as of March 31, 2018 (together with the corresponding percentage of the fair value of our total portfolio of investments):

	As of March 31, 2018					
	Investments at Amortized Cost	Percentage of Amortized Cost		Investments at Fair Value	Percentage of Fair Value	
Senior Secured Loans	$1,250,000	16.5	%	$ 500,000	5.9	%
Preferred Stock	1,320,214	17.4		2,418,623	28.5	
Common Stock	3,880,306	51.0		4,528,546	53.4	
Warrants	679	—		21,429	0.3	
Other Equity	1,151,019	15.1		1,013,629	11.9	
Total	$7,602,218	100.0	%	$ 8,482,227	100.0	%

The following table shows the composition of our investment portfolio by major class, at amortized cost and fair value, as of December 31, 2017 (together with the corresponding percentage of the fair value of our total portfolio of investments):

	As of December 31, 2017					
	Investments at Amortized Cost	Percentage of Amortized Cost		Investments at Fair Value	Percentage of Fair Value	
Senior Secured Loans	$1,250,000	17.8	%	$ 500,000	6.9	%
Preferred Stock	1,320,214	19.0		2,420,659	33.4	
Common Stock	3,278,833	46.8		3,263,715	45.1	
Warrants	679	—		42,857	0.6	
Other Equity	1,151,019	16.4		1,013,629	14.0	

Total	$7,000,745	100.0	%	$ 7,240,860	100.0	%

The following table shows the composition of our investment portfolio by industry grouping, based on fair value as of March 31, 2018:

	As of March 31, 2018		
	Investments at Fair Value	**Percentage of Fair Value**	
Advertising	$ 21,429	0.3	%
Business Services	223,168	2.6	
Consumer	458,520	5.4	
Education	149,844	1.8	
Financial	914,957	10.8	
Healthcare	1,004,540	11.8	
Industrial Goods	6,885	0.1	
Information Technology	917,199	10.8	
Leisure & Hospitality	2,520,226	29.7	
Oil & Gas	625,629	7.4	
Publishing	1,639,830	19.3	
Total	$ 8,482,227	100.0	%

The following table shows the composition of our investment portfolio by industry grouping, based on fair value as of December 31, 2017:

	As of December 31, 2017		
	Investments at Fair Value	**Percentage of Fair Value**	
Advertising	$ 42,857	0.6	%
Consumer	447,942	6.2	
Education	142,000	2.0	
Financial	941,517	13.0	
Healthcare	513,862	7.1	
Industrial Goods	12,240	0.2	
Information Technology	896,009	12.4	
Leisure & Hospitality	2,520,226	34.8	
Oil & Gas	488,629	6.7	
Publishing	1,235,578	17.0	
Total	$ 7,240,860	100.0	%

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March 31, 2018

We do not “control,” and we are not an “affiliate” (as each of those terms is defined in the 1940 Act), of any of our portfolio companies as of March 31, 2018. Under the 1940 Act, we would generally be presumed to “control” a portfolio company if we owned more than 25% of its voting securities, and be an “affiliate” of a portfolio company if we owned at least 5% and up to 25% of its voting securities.

NOTE 4 – FAIR VALUE OF FINANCIAL INSTRUMENTS

General information: Accounting guidance establishes a hierarchal disclosure framework that prioritizes and ranks the level of market price observability of inputs used in measuring investments at fair value. Observable inputs must be used when available. Observable inputs are inputs that market participants would use in valuing the asset or liability based on market data obtained from independent sources. Unobservable inputs are inputs that reflect our assumptions about the factors market participants would use in valuing the asset or liability based upon the best information available. Assets and liabilities measured at fair value are to be categorized into one of the three hierarchy levels based on the relative observability of inputs used in the valuation. The three levels are defined as follows:

- **Level 1:** Observable inputs based on quoted prices (unadjusted) in active markets for identical assets or liabilities.

- **Level 2:** Observable inputs based on quoted prices for similar assets and liabilities in active markets, or quoted prices for identical assets and liabilities in inactive markets.

- **Level 3:** Unobservable inputs that reflect an entity’s own assumptions about what inputs a market participant would use in pricing the asset or liability based on the best information available in the circumstances.

Our valuation policy and procedures: Under our valuation policies and procedures, we evaluate the source of inputs, including any markets in which our investments are trading, and then apply the resulting information in determining fair value. For our Level 1 investment assets, our valuation policy generally requires us to use a market approach, considering the last quoted closing price of a security we own that is listed on a securities exchange, and in a case where a security we own is listed on an over-the-counter market, to average the last quoted bid and ask price on the most active market on which the security is quoted. In the case of traded debt securities the prices for which are not readily available, we may value those securities using a present value approach, at their weighted-average yield to maturity.

The estimated fair value of our Level 3 investment assets is determined on a quarterly basis by the Valuation Committee of our Board of Directors, pursuant to our written Valuation Policy and Procedures. These policies and procedures generally require that we value our Level 3 equity investments at cost plus any accrued interest, unless circumstances warrant a different approach. Our Valuation Policy and Procedures provide examples of these circumstances, such as when a portfolio company has engaged in a subsequent financing of more than a *de minimis* size involving sophisticated investors (in which case we may use the price involved in that financing as a determinative input absent other known factors), or when a portfolio company is engaged in the process of a transaction that we determine is reasonably likely to occur (in which case we may use the price involved in the pending transaction as a determinative input absent other known factors). Other situations identified in our Valuation Policy and Procedures that may serve as input supporting a change in the valuation of our Level 3 equity investments include (i) a third-party valuation conducted by an independent and qualified professional, (ii) changes in the performance of long-term financial prospects of the portfolio company, (iii) a subsequent financing that changes the distribution rights associated with the equity security we hold, or (iv) sale transactions involving comparable companies, but only if further supported by a third-party valuation conducted by an independent and qualified professional.

When valuing preferred equity investments, we generally view intrinsic value as a key input. Intrinsic value means the value of any conversion feature (if the preferred investment is convertible) or the value of any liquidation or other preference. Discounts to intrinsic value may be applied in cases where the issuer’s financial condition is impaired or, in cases where intrinsic value relating to a conversion is determined to be a key input, to account for resale restrictions applicable to the securities issuable upon conversion.

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NOTES TO FINANCIAL STATEMENTS (UNAUDITED)

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When valuing warrants, our Valuation Policy and Procedures indicate that value will generally be the difference between closing price of the underlying equity security and the exercise price, after applying an appropriate discount for restriction, if applicable, in situations where the underlying security is marketable. If the underlying security is not marketable, then intrinsic value will be considered consistent with the principles described above. Generally, “out-of-the-money” warrants will be valued at cost or zero.

For non-traded (Level 3) debt securities with a residual maturity less than or equal to 60 days, the value will generally be based on a present value approach, considering the straight-line amortized face value of the debt unless justification for impairment exists.

On a quarterly basis, our management provides members of our Valuation Committee with (i) valuation reports for each portfolio investment (which reports include our cost, the most recent prior valuation and any current proposed valuation, and an indication of the valuation methodology used, together with any other supporting materials); (ii) Mill City Ventures’ bank and other statements pertaining to our cash and cash equivalents; (iii) quarter- or period-end statements from our custodial firms holding any of our portfolio investments; and (iv) recommendations to change any existing valuations of our portfolio investments or hierarchy levels for purposes of determining the fair value of such investments based upon the foregoing. The committee then discusses these materials and, consistent with the policies and approaches outlined above, makes final determinations respecting the valuation and hierarchy levels of our portfolio investments.

We made no changes to our Valuation Policy and Procedures during the reporting period.

Level 3 valuation information: Due to the inherent uncertainty in the valuation process, the estimate of the fair value of our investment portfolio as of March 31, 2018 may differ materially from values that would have been used had a readily available market for the securities existed.

The following table presents the fair value measurements of our portfolio investments by major class, as of March 31, 2018, according to the fair value hierarchy:

	As of March 31, 2018			
	Level 1	Level 2	Level 3	Total
Senior Secured Loans	$-	$-	$500,000	$500,000
Preferred Stock	-	98,397	2,320,226	2,418,623
Common Stock	4,528,546	-	-	4,528,546
Warrants	-	21,429	-	21,429
Other Equity	-	-	1,013,629	1,013,629
Total	$4,528,546	$119,826	$3,833,855	$8,482,227

The following table presents the fair value measurements of our portfolio investments by major class, as of December 31, 2017, according to the fair value hierarchy

	As of December 31, 2017			
	Level 1	Level 2	Level 3	Total
Senior Secured Loans	$-	$-	$500,000	$500,000
Preferred Stock	-	100,433	2,320,226	2,420,659
Common Stock	3,262,915	800	-	3,263,715
Warrants	-	42,857	-	42,857
Other Equity	-	-	1,013,629	1,013,629
Total	$3,262,915	$144,090	$3,833,855	$7,240,860

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March 31, 2018

The following table presents a reconciliation of the beginning and ending fair value balances for our Level 3 portfolio investment assets for the three months ended March 31, 2018:

	Senior Secured Loans	Preferred Stock	Common Stock	Warrants	Other Equity
Balance as of December 31, 2017	$ 500,000	$ 2,320,226	$ -	$ -	$ 1,013,629
Net change in unrealized appreciation (depreciation)	-	-	-	-	-
Purchases and other adjustments to cost	-	-	-	-	-
Sales and redemptions	-	-	-	-	-
Net realized gain	-	-	-	-	-
Balance as of March 31, 2018	$ 500,000	$ 2,320,226	$ -	$ -	$ 1,013,629

The net change in unrealized depreciation for the three months ended March 31, 2018 attributable to Level 3 portfolio investments still held as of March 31, 2018 is $0.

The following table lists our level 3 investments held as of March 31, 2018 and the unobservable inputs used to determine their valuation:

	Security Type	3/31/18 FMV	Unobservable Inputs
Mix 1 Life, Inc.	Loans (Secured)	$ —	company is in default on its debt to us
Bravo Financial LLC	Loans (Secured)	500,000	cost
Insite Software Solutions, Inc	Warrants	—	company is a going-concern
Tzfat Spirits of Israel, LLC	Other Equity	25,000	last funding secured by company
MAX 4G, Inc.	Preferred Stock	300,000	last funding secured by company
Bitesquad.com LLC	Preferred Stock	2,020,226	last funding secured by company
DBR Enclave US Investors, LLC	Other Equity	500,000	cost
	Other Equity	488,629	

Northern Capital Partners I, LP			company is generating substantial revenue and allocated income
Southern Plains Resources, Inc.	Common Stock	—	company has substantially ceased operations
		$ 3,833,855	

The following table presents a reconciliation of the beginning and ending fair value balances for our Level 3 portfolio investment assets for the period ended December 31, 2017:

	Senior Secured Loans	Preferred Stock	Common Stock	Warrants	Other Equity
Balance as of January 1, 2017	$ 680,000	$ 3,047,011	$ -	$ -	$ 513,629
Net change in unrealized appreciation	(97,305)	138,321	-	-	-
Purchases and other adjustments to cost	10,000	-	-	-	500,000
Sales and redemptions	(182,695)	(746,225)	-	(5,884)	-
Net realized gain	90,000	(118,881)	-	5,884	-
Balance as of December 31, 2017	$ 500,000	$ 2,320,226	$ -	$ -	$ 1,013,629

The net change in unrealized appreciation for the year ended December 31, 2017 attributable to Level 3 portfolio investments still held as of December 31, 2017 was $180,000, and is included in net change in unrealized appreciation (depreciation) on investments on the statement of operations.

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MILL CITY VENTURES III, LTD.

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March 31, 2018

The following table lists our level 3 investments held as of December 31, 2017 and the unobservable inputs used to determine their valuation:

	Security Type	12/31/17 FMV	Unobservable Inputs
Mix 1 Life, Inc.	Loans (Secured)	$ —	company is in default on its debt to us
Bravo Financial LLC	Loans (Secured)	500,000	cost
Insite Software Solutions, Inc	Warrants	—	company is a going-concern
Tzfat Spirits of Israel, LLC	Other Equity	25,000	last funding secured by company
MAX 4G, Inc.	Preferred Stock	300,000	last funding secured by company
Bitesquad.com LLC	Preferred Stock	2,020,226	last funding secured by company
DBR Enclave US Investors, LLC	Other Equity	500,000	cost
Northern Capital Partners I, LP	Other Equity	488,629	last K-1 valuation received
Southern Plains Resources, Inc.	Common Stock	—	company in default on its balance sheet debt
		$ 3,833,855	

NOTE 5 – RELATED-PARTY TRANSACTIONS

We maintain 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 regulations applicable to BDCs generally describe as “affiliate transactions.” Nevertheless, from time to time we may hold investments in portfolio companies in which certain members of our management, our Board of Directors, or significant shareholders of ours, are also directly or indirectly invested. Our Board of Directors has adopted a policy to require our disclosure of these instances in our periodic filings with the SEC. Our related-party transactions requiring disclosure under this policy are:

- Mr. Joseph A. Geraci, II, our Chief Financial Officer, and Mr. Douglas M. Polinsky, our Chief Executive Officer, hold direct and indirect interests in the common stock of Southern Plains Resources, Inc., a company in which we made investments in common stock in each of March and July 2013.

- A former director of our company, Christopher Larson, had a direct interest in Mix 1 Life, Inc. and served as that company’s Chief Financial Officer at the time of a portfolio investment we made in secured convertible debt of Mix 1 Life (together with common stock purchase warrants) in February 2014. In June 2014, Mr. Larson became a director of Mix 1 Life. In August 2014, we exercised our common stock purchase warrant on a cashless basis for the purchase of Mix 1 Life common stock. In March 2015, we invested in additional secured debt of Mix 1 Life. Mr. Larson resigned from his position as a director of Mill City Ventures in November 2015.

Lantern Advisors, LLC is a limited liability company equally owned by Messrs. Geraci and Polinsky, and owns a cashless warrant to purchase up to 153,846 shares of Creative Realities, Inc. at a price of $0.70 per share through July 14, 2019. We made an initial investment in secured convertible debt of Creative Realities (together with common stock purchase warrants) in February 2015, and then a subsequent investment in secured convertible debt of Creative Realities (together with common stock purchase warrants) in December 2015. In December 2015, we also exchanged our common stock purchase warrant obtained in February 2015 for shares of Creative Realities common stock.

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MILL CITY VENTURES III, LTD.

NOTES TO FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2018

NOTE 6 – COMMITMENTS AND CONTINGENCIES

We have 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 base rent expense for the three months ended March 31, 2018 and 2017 was $11,345 and $11,345, respectively. The table below sets forth the required annual minimum lease payments:

Year	Amount
2018	$34,173
Total	$34,173

NOTE 7 – INCOME TAXES

We plan to be taxed as a regulated investment company, or “RIC,” and intend to comply with the requirements of the Code applicable to RICs. Currently, however, we have not elected to be treated as a RIC. Upon our election to be taxed as a RIC, we will be required to distribute at least 90% of our investment company taxable income, and we intend at that time to distribute to shareholders (or retain through a deemed distribution) all of our investment company taxable income and net capital gain. Based on the foregoing, 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 – SHAREHOLDERS’ EQUITY

At March 31, 2018, we had 11,067,402 shares of common stock issued and outstanding.

NOTE 9 – PER-SHARE INFORMATION

Basic net gain (loss) per common share is computed by dividing net gain (loss) by the weighted-average number of 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 is set forth below:

	For the Three Months Ended March 31,	
	2018	2017
Numerator: Net increase (decrease) in net asset value resulting from operations	$ 539,590	$ (20,518)
Denominator: Weighted-average number of common shares outstanding	11,067,402	12,151,493
Basic and diluted net gain (loss) per common share	$ .05	$ .00

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MILL CITY VENTURES III, LTD.

NOTES TO FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2018

NOTE 10 – FINANCIAL HIGHLIGHTS

The following is a schedule of financial highlights for the three months ended March 31, 2018 through 2014:

	Three Months Ended March 31, 2018	March 31, 2017	March 31, 2016	March 31, 2015	March 31, 2014
Per Share Data [(1)]					
Net asset value at beginning of period	$0.87	0.77	0.72	0.94	0.86
Net investment income (loss)	(0.01)	(0.01)	0.00	0.00	(0.01)
Net realized and unrealized gains (losses)	0.06	0.01	0.00	0.01	0.07
Net asset value at end of period	$0.92	0.77	0.72	0.95	0.92
Ratio / Supplemental Data					
Per share market value of investments at end of period	$0.76	0.46	0.46	0.72	0.34
Shares outstanding at end of period	11,067,402	12,151,493	12,151,493	12,151,493	12,169,422
Average weighted shares outstanding for the period	11,067,402	12,151,493	12,151,493	12,151,493	12,169,422
Net assets at end of period	$10,168,805	9,366,890	8,720,448	11,626,869	11,296,396
Average net assets [(2)]	$9,770,410	9,563,916	8,718,010	11,561,049	10,766,742
Total investment return	5.75%	0.00%	0.00%	1.06%	6.98%
Portfolio turnover rate (3)	0.80%	7.26%	8.25%	3.86%	5.79%
Ratio of operating expenses to average net assets [(3)]	(7.52)%	(6.86)%	(6.65)%	(5.60)%	(5.58)%
Ratio of net investment income (loss) to average net assets [(3)]	(6.16)%	(5.38)%	(2.78)%	0.02%	(4.06)%
Ratio of realized gains (losses) to average net assets [(3)]	2.17%	33.82%	(22.92)%	5.25%	7.79%

(1) Per-share data was derived using the ending number of shares outstanding for the period.

(2) Based on the monthly average of net assets as of the beginning and end of each period presented.

(3) Ratios are annualized.

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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 (MD&A) is intended to provide a reader of our financial statements with a narrative from the perspective of management on our financial condition, results of operations, liquidity and certain other factors that may affect our future results. In addition, unless expressly stated otherwise, the comparisons presented in this MD&A refer to the same period in the prior year. Our MD&A is presented in seven sections:

- Overview
- Portfolio and Investment Activity
- Results of Operations
- Financial Condition
- Critical Accounting Estimates
- Off-Balance Sheet Arrangements
- Forward Looking Statements

OVERVIEW

Mill City Ventures III, Ltd. is an investment company incorporated in the State of Minnesota on January 10, 2006. In this report, we generally refer to Mill City Ventures III, Ltd. in the first person "we." On occasion, we refer to our company in the third person as "Mill City Ventures" or the "company."

We are an internally managed closed-end non-diversified management investment company. We have elected to be regulated as a business development company, or "BDC," under the Investment Company Act of 1940 (the "1940 Act"). To date, we have not made an election to be treated as a regulated investment company, or "RIC," under the Internal Revenue Code of 1986 (the "Code").

We primarily focus on investing in or lending to privately held and small-cap publicly traded U.S. companies, and making managerial assistance available to such companies. These investments are typically structured as purchases of preferred or common stock, investment contracts, or loans evidenced by promissory notes that may be convertible into stock by their terms or that may be accompanied by the issuance to us of warrants or similar rights to purchase stock. Our investments may be made for purposes of financing acquisitions, recapitalizations, buyouts, organic growth and working capital. Our revenues relate to the gain we realize from the sale of securities we purchase, and to dividends and interest we derive from those securities. Our investment objective is to generate both current income and capital appreciation that ultimately result in gains.

Our principal sources of income are interest and dividends we earn on our investments, and proceeds from the sale or redemption of our investments. Our statements of operations also reflect gain from increases in the carrying value of our investments (i.e., unrealized appreciation). Our principal expenses relate to operating expenses, the largest components of which are generally professional fees, payroll, occupancy, and insurance expenses. Our statements of operations also reflect loss from decreases in the carrying value of our investments (i.e., unrealized depreciation).

As a BDC, we are required to comply with certain regulatory requirements. For example, we must invest at least 70% of our total assets in “qualifying assets,” including securities of private or small-cap publicly traded U.S. companies and cash, cash equivalents, U.S. government securities and high quality debt investments that mature in one year or less. We may from time to time invest up to 30% of our assets opportunistically in other types of investments, including the securities of larger public companies and foreign securities. In addition, we will be permitted, under certain 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.

Our MD&A should be read in conjunction with our Annual Report on Form 10-K for the year ended December 31, 2017, as well as our reports on Forms 10-Q and 8-K and other publicly available information. All amounts herein are unaudited. In addition, the following discussion of our results of operations and financial condition should be read in the context of this overview.

PORTFOLIO AND INVESTMENT ACTIVITY

During the three months ended March 31, 2018, we made $628,252 of investments in portfolio companies and had $78,531 of redemptions and repayments, resulting in net investments at amortized cost of $7,602,218 for the period.

During the three months ended March 31, 2017, we made $694,120 of investments in portfolio companies and had $2,321,114 of redemptions and repayments, resulting in net investments at amortized cost of $6,483,185 for the period.

Our portfolio composition by major class, based on fair value at March 31, 2018, was as follows:

	Investments at Fair Value	Percentage of Fair Value	
Senior Secured Loans	$ 500,000	5.9	%
Unsecured Loans	-	-	
Equity/Other	7,982,227	94.1	
Total	$ 8,482,227	100.0	%

RESULTS OF OPERATIONS

Our operating results for the three months ended March 31, 2018 and March 31, 2017 were as follows:

	For the three months ended March 31, 2018		2017	
Total investment income	$ 34,525		$ 36,564	
Total expenses	(186,581	)	(166,214	)
Net investment loss	$ (152,056	)	$ (129,650	)

Investment Income

We generate revenue primarily in the form of interest income and capital gains, if any, on the debt securities we own. We may also generate revenue from dividends and capital gains on equity investments we make, if any, or on warrants or other equity interests that we may acquire. In some cases, the interest on our investments may accrue or be paid in the form of additional debt. The principal amount of the debt instruments, together with any accrued but unpaid interest thereon, will generally become due at the maturity date of those debt instruments. We may also generate revenue in the form of commitment, origination, structuring, diligence, or consulting fees. Any such fees will be recognized as earned.

For the three months ended March 31, 2018, our total investment income was $34,525, and was attributable to interest income from two eligible portfolio companies, Bravo Financial, LLC and DBR Enclave LLC, and dividend payments received on account of investments in two eligible portfolio companies - OTC Markets Group Cl A, and Simulations Plus, Inc.

For the three months ended March 31, 2017, our total investment income was $36,564, and was attributable to interest income from two eligible portfolio companies, Bravo Financial, LLC and DBR Enclave LLC, and dividend payments received on account of investments in five eligible portfolio companies - OTC Markets Group Cl A, Simulations Plus, Inc., Tessco Technologies, Inc., Escalade Inc., and National American University Holdings, Inc., and dividends received on account of investments in three non-eligible portfolio companies.

Operating Expenses

The composition of our operating expenses for the three months ended March 31, 2018 and March 31, 2017 was as follows:

Expense item	Three months ended March 31, 2018	Three months ended March 31, 2017
Professional fees	$ 60,281	$ 66,736
Payroll	61,053	41,358
Occupancy	22,755	19,822
Insurance	18,891	17,446
Directors' fees	15,000	15,000
Depreciation and amortization	2,671	2,748
Other general and administrative	5,930	3,104
Total	$ 186,581	$ 166,214

Net Realized Gain from Investments

For the three months ended March 31, 2018, we had $78,531 of principal repayments, resulting in $51,752 of realized gains. For the three months ended March 31, 2017, we had $2,321,114 of principal repayments, resulting in $712,271 of realized gains.

Net Change in Unrealized Appreciation (Depreciation) on Investments

For the three months ended March 31, 2018, our investments had $639,894 of unrealized appreciation. For the three months ended March 31, 2017, our investments had $603,139 of unrealized depreciation.

Changes in Net Assets from Operations

For the three months ended March 31, 2018, we recorded a net increase in net assets from operations of $539,590. Based on the weighted-average number of shares of common stock outstanding for the three months ended March 31, 2018, our per-share net increase in net assets from operations was $0.05. For the three months ended March 31, 2017, we recorded a net decrease in net assets from operations of $20,518. Based on the weighted-average number of shares of common stock outstanding for the three months ended March 31, 2017, our per-share net decrease in net assets from operations was $0.00.

Cash Flows for the Three Months Ended March 31, 2018 and 2017

The level of cash flows used in or provided by operating activities is affected by the timing of purchases, redemptions and repayments of portfolio investments, among other factors. For the three months ended March 31, 2018, net cash used in operating activities was $393,046. Cash flows used in operating activities for the three months ended March 31, 2018 were primarily related to purchases of investments of $628,252, offset mostly by redemptions and repayments of investments totaling $78,531. For the three months ended March 31, 2017, net cash provided in operating activities was $1,726,115. Cash flows provided in operating activities for the three months ended March 31, 2017 were primarily related to redemptions and repayments of $2,321,114 offset mostly by purchases of investments totaling $694,120.

FINANCIAL CONDITION

As of March 31, 2018, we had cash of $1,765,268, a decrease of $393,046 from December 31, 2017. The primary use of our existing funds and any funds raised in the future is expected to be for our investments in portfolio companies, cash distributions to our shareholders or for other general corporate purposes, including paying for operating expenses or debt service to the extent we borrow or issue senior securities. Pending investment in portfolio companies, 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." As of the date of this filing, we expect that substantially all of our temporary investments will be redeployed into portfolio company investments by December 31, 2018.

To the extent our Board of Directors determines in the future, based on our financial condition and capital market conditions, that additional capital would allow us to take advantage of additional investment opportunities, we may seek to raise additional equity capital or to engage in borrowing, subject to the limitations on borrowing applicable to BDCs.

RELATED-PARTY TRANSACTIONS

See Note 5 to our Financial Statements for disclosure of our related-party transactions and potential conflicts of interest.

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CRITICAL ACCOUNTING ESTIMATES

Our financial statements are prepared in conformity with accounting principles generally accepted in the United States of America, or U.S. GAAP, which requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Critical accounting policies are those that require the application of management's most difficult, subjective or complex judgments, often because of the need to make estimates about the effect of matters that are inherently uncertain and that may change in subsequent periods.

In preparing the financial statements, management will make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting periods. In preparing the financial statements, management also will utilize available information, including our past history, industry standards and the current economic environment, among other factors, in forming its estimates and judgments, giving due consideration to materiality. Actual results will almost certainly differ from these estimates. In addition, other companies may utilize different estimates, which may impact the comparability of our results of operations to those of companies in similar businesses. As our expected operating results occur, we will describe additional critical accounting policies in the notes to our financial statements. Our most critical accounting policies relate to the valuation of our portfolio investments, and revenue recognition. For more information, see Note 2 "Significant Accounting Policies."

OFF-BALANCE-SHEET ARRANGEMENTS

During the three months ended March 31, 2018, we did not engage in any off-balance sheet arrangements as described in Item 303(a)(4) of Regulation S-K.

FORWARD-LOOKING STATEMENTS

Some of the statements made in this section of our report are forward-looking statements based on our management's current expectations for our company. These expectations involve assumptions and are subject to substantial risks and uncertainties that 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, and can ordinarily be identified by terminology such as "may," "will," "should," "expects," "plans," "anticipates," "could," "in "targets," "projects," "contemplates," "believes," "estimates," "predicts," "potential" or "continue" or the negative of these terr other similar words. Important assumptions include our ability to identify and consummate new investments, achieve certain margins and levels of profitability, the availability of any needed additional capital, and the ability to maintain compliance with regulations applicable to us. Some of the forward-looking statements contained in this report relate to, and are based our current assumptions regarding, the following:

- our future operating results;
- our business prospects and the prospects of our portfolio companies;
- the outcome of compliance inspections conducted from time to time by the SEC's Office of Compliance and Inspections;
- the success of our investments;
- our relationships with third parties;
- the dependence of our 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 BDC and to be taxed as a RIC;
- 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. 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 30, 2018 (related to our year ended December 31, 2017) and in particular the section thereof entitled "Risk Factors." Because of the significant uncertainties inherent in forward-looking statements pertaining to our company, the inclusion of those statements 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 filing. 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.

ITEM 4. 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, 2018, 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, 2018.

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 Number		Description
3.1		Amended and Restated Articles of Incorporation (incorporated by reference to Exhibit 3.1 to the registrant's Current Report on Form 8-K filed January 23, 2013)
3.2		Amended and Restated Bylaws of Mill City Ventures III, Ltd. (incorporated by reference to Exhibit 3.2 to the registrant's registration statement on Form 10-SB filed on January 29, 2008)
31.1	*	Section 302 Certification of the Chief Executive Officer
31.2	*	Section 302 Certification of the Chief Financial Officer
32.1	*	Certification of Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. §1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

* Filed herewith

SIGNATURES

Pursuant to the requirements of the Securities and 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.

Date: May 11, 2018 By: /s/ Douglas M. Polinsky
Douglas M. Polinsky
Chief Executive Officer

Date: May 11, 2018 By: /s/ Joseph A. Geraci, II
Joseph A. Geraci, II
Chief Financial Officer