

Mill City Ventures III, Ltd  
Form 10-K/A  
August 17, 2016

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**

WASHINGTON, D.C. 20549

AMENDMENT NO. 1 TO

FORM 10-K/A

(Mark One)

**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE  
ACT OF 1934**

**For the fiscal year ended December 31, 2015**

**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 of incorporation) (I.R.S. Employer Identification No.)

**328 Barry Ave. S. #210**  
**Wayzata, Minnesota**                      **55391**  
(Address of principal executive offices) (Zip Code)

Former name, former address and former fiscal year, if changed since last report

Registrant's telephone number, including area code: (952) 479-1923

**Securities registered pursuant to Section 12(b) of the Act:**

**Title of Each Class Name of Each Exchange on which Registered**

None

**Securities registered pursuant to Section 12(g) of the Act:**

Common stock, \$0.001 par value per share

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

Yes  No

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 the filing requirements for the past 90 days.  Yes  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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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 definition of "large accelerated filer," "accelerated filer," "non-accelerated filer," and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one)

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

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

The aggregate market value of the voting stock held by persons other than officers, directors and more than 5% shareholders of the registrant as of August 15, 2016, there were 12,151,493 shares of the registrant's common stock, \$0.001 par value, outstanding.

**DOCUMENTS INCORPORATED IN PART BY REFERENCE**

None.

## NOTE OF EXPLANATION

We are filing this Amendment No. 1 to Annual Report on Form 10-K to amend (i) the audit opinion of our independent registered public accounting firm for the purpose of adding language relating to the confirmation of our investments, (ii) our Schedule of Investments and our financial highlights summary to conform to requirements set forth in Regulation S-X and otherwise, and (iii) attach new certifications on Exhibits 31.1, 31.,2, and 32. All of these amendments affect Item 8 to our Annual Report on Form 10-K originally filed on March 30, 2016 (the “Original 10-K”). As a result, the entirety of Item 8 is set forth in this amendment. This amendment amends no other portions of the Original 10-K other than as set forth herein.

### Mill City Ventures III, Ltd.

#### Form 10-K/A

#### Table of Contents

## PART II

|  |             |
|--|-------------|
| Item 8. Financial Statement and Supplemental Data  | <u>Page</u> |
| Report of Independent Registered Public Accounting Firm  | 1           |
| Balance Sheets — December 31, 2015 and December 31, 2014   | 2           |
| Statements of Operations — Years ended December 31, 2015 and December 31, 2014                     | 3           |
| Statements of Shareholders’ Equity (Deficit) — Years ended December 31, 2015 and December 31, 2014 | 4           |
| Statements of Cash Flows — Years ended December 31, 2015 December 31, 2014                         | 5           |
| Notes to Financial Statements  | 14          |
| <br>SIGNATURES   | <br>25      |

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders, Audit Committee and Board of Directors

Mill City Ventures III, Ltd.

Wayzata, Minnesota

We have audited the accompanying balance sheets of Mill City Ventures III, Ltd. as of December 31, 2015 and 2014, and the related statements of operations, shareholders' equity and cash flows for the year ended December 31, 2015, and December 31, 2014 and the financial highlights for each of the three years in the period then ended. These financial statements and financial highlights are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of its internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the company's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management as well as the overall financial statement presentation. Our procedures included confirmation of investments as of December 31, 2015 and 2014, by correspondence with the custodian, loan agents or borrowers. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements and financial highlights referred to above, including the schedule of investments, present fairly, in all material respects, the financial position of Mill City Ventures III, Ltd. as of December 31, 2015 and 2014 and the results of their operations and cash flows for the years ended December 31, 2015 and 2014 and the financial highlights for each of the three years in the period then ended, in conformity with U.S. generally accepted accounting principles.

/s/ Baker Tilly Virchow Krause, LLP

Minneapolis, Minnesota

March 31, 2016

Reissued August 15, 2016

Table of Contents 1

## Mill City Ventures III, Ltd.

## Balance Sheets

|   | December<br>31,<br>2015 | December<br>31,<br>2014 |
|---|-------------------------|-------------------------|
| <b>ASSETS</b>   |                         |                         |
| Investments, at fair value  |                         |                         |
| Non-control/Non-affiliate investments (cost of \$7,218,131 and \$5,797,518)   | \$5,747,808             | \$7,171,509             |
| Cash  | 2,980,659               | 4,105,911               |
| Prepaid expenses  | 43,808                  | 49,623                  |
| Receivable from sale of investments   | —                       | 82,103                  |
| Interest and dividends receivable   | 23,840                  | 59,794                  |
| Leasehold improvements, net   | 23,773                  | 31,882                  |
| Property and equipment, net   | 14,222                  | 18,962                  |
| Total Assets  | \$8,834,110             | \$11,519,784            |
| <b>LIABILITIES</b>  |                         |                         |
| <b>Current Liabilities</b>  |                         |                         |
| Accounts payable  | \$10,431                | \$36,098                |
| Payable for purchase of investments   | 65,622                  | —                       |
| Deferred interest income  | 5,645                   | —                       |
| Deferred rent   | 11,124                  | 9,996                   |
| Total Current Liabilities   | 92,822                  | 46,094                  |
| Total Liabilities   | 92,822                  | 46,094                  |
| <b>SHAREHOLDERS' EQUITY</b>   |                         |                         |
| Common Stock, \$.001 par value: Authorized 250,000,000 shares: Issued and outstanding 12,151,493 and 12,169,422 shares. | 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   | (1,099,927 )            | (1,028,423 )            |
| Accumulated undistributed net realized gains on investment transactions   | 601,392                 | 417,976                 |
| Net unrealized appreciation/(depreciation) in value of investments  | (1,470,323 )            | 1,373,991               |
| Total Shareholders' Equity  | 8,741,288               | 11,473,690              |
| Total Liabilities and Shareholders' Equity  | \$8,834,110             | \$11,519,784            |

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



Mill City Ventures III, Ltd.

## Statements of Operations

|  | Year Ended<br>December<br>31,<br>2015 | Year Ended<br>December<br>31,<br>2014 |
|--|---------------------------------------|---------------------------------------|
| Investment Income  |                                       |                                       |
| Interest income  | \$478,331                             | \$239,425                             |
| Dividend income  | 89,751                                | 100,926                               |
| Total Investment Income  | 568,082                               | 340,351                               |
| Operating Expenses:  |                                       |                                       |
| Professional fees  | 206,292                               | 157,274                               |
| Payroll expense  | 162,861                               | 370,976                               |
| Insurance expense  | 89,421                                | 107,735                               |
| Occupancy  | 91,217                                | 82,058                                |
| Director's fees  | 55,000                                | 60,000                                |
| Depreciation and amortization  | 12,849                                | 12,658                                |
| Other general and administrative expenses                                  | 21,946                                | 8,725                                 |
| Total Operating Expenses   | 639,586                               | 799,426                               |
| Net Investment Loss  | \$(71,504 )                           | \$(459,075 )                          |
| Realized and Unrealized Gain (Loss) on Investments                         |                                       |                                       |
| Net realized gain on investments   | \$183,416                             | \$289,439                             |
| Net change in unrealized appreciation (depreciation) on investments        | \$(2,844,314 )                        | \$1,136,098                           |
| Net Realized and Unrealized Gain (Loss) on Investments                     | (2,660,898 )                          | 1,425,537                             |
| Net Increase (Decrease) in Net Asset Value Resulting from Operations       | \$(2,732,402 )                        | \$966,462                             |
| Net Increase (Decrease) in Net Assets Resulting from Operations per share: |                                       |                                       |
| Basic and diluted  | \$(0.22 )                             | \$0.08                                |
| Weighted-average number of common shares outstanding                       | 12,151,493                            | 12,166,598                            |

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

Table of Contents 3

Mill City Ventures III, Ltd.

## Statements of Shareholders' Equity

For the years ended December 31, 2015, 2014 and 2013

|  | Common Stock |          | Additional<br>Paid In<br>Capital | Accumulated<br>Deficit | Accumulated<br>Investment<br>Loss | Accumulated<br>Undistributed<br>Net<br>Realized<br>Gains on<br>Investments<br>Transactions | Accumulated<br>Undistributed<br>Net<br>Unrealized<br>Appreciation<br>in value of<br>Investments | Total<br>Shareholders'<br>Equity |
|--|--------------|----------|----------------------------------|------------------------|-----------------------------------|--|---|----------------------------------|
|  | Shares       | Amount   | Capital                          | Deficit                | Loss                              | Transactions   | Investments   | Equity                           |
| Balance as of<br>December 31,<br>2013  | 12,169,422   | \$12,169 | \$11,875,571                     | \$(1,159,665)          | \$(572,675)                       | \$128,537  | \$237,893   | \$10,521,830                     |
| Repurchase of<br>common<br>stock for cash<br>of \$0.83 per<br>share on<br>August 29,<br>2014   | (2,973)      | (3)      | (2,970)                          | —                      | 509                               | —  | —   | (2,464)                          |
| Repurchase of<br>common<br>stock for cash<br>of \$0.80 per<br>share on<br>September 3,<br>2014 | (4,510)      | (5)      | (4,505)                          | —                      | 890                               | —  | —   | (3,620)                          |
| Repurchase of<br>common<br>stock for cash<br>of \$0.84 per<br>share on<br>December 19,<br>2014 | (10,446)     | (10)     | (10,436)                         | —                      | 1,928                             | —  | —   | (8,218)                          |
| Undistributed<br>investment<br>loss  | —            | —        | —                                | —                      | (459,075)                         | —  | —   | (459,075)                        |
| Undistributed<br>net realized<br>gains on  | —            | —        | —                                | —                      | —                                 | 289,439  | —   | 289,439                          |

investment  
transactions

|   |            |          |              |               |               |           |               |              |
|---|------------|----------|--------------|---------------|---------------|-----------|---------------|--------------|
| Appreciation<br>in value of<br>investments                              | —          | —        | —            | —             | —             | —         | 1,136,098     | 1,136,098    |
| Balance as of<br>December 31,<br>2014                                   | 12,151,493 | \$12,151 | \$11,857,660 | \$(1,159,665) | \$(1,028,423) | \$417,976 | \$1,373,991   | \$11,473,690 |
| Undistributed<br>investment<br>loss                                     | —          | —        | —            | —             | (71,504 )     | —         | —             | (71,504 )    |
| Undistributed<br>net realized<br>gains on<br>investment<br>transactions | —          | —        | —            | —             | —             | 183,416   | —             | 183,416      |
| Depreciation<br>in value of<br>investments                              | —          | —        | —            | —             | —             | —         | (2,844,314)   | (2,844,314)  |
| Balance as of<br>December 31,<br>2015                                   | 12,151,493 | \$12,151 | \$11,857,660 | \$(1,159,665) | \$(1,099,927) | \$601,392 | \$(1,470,323) | \$8,741,288  |

Table of Contents 4

Mill City Ventures III, Ltd.

## Statements of Cash Flows

|   | Year Ended<br>December<br>31,<br>2015 | Year Ended<br>December<br>31,<br>2014 |
|---|---------------------------------------|---------------------------------------|
| Cash flows from operating activities:   |                                       |                                       |
| Net increase (decrease) in net asset value resulting from operations  | \$(2,732,402)                         | \$966,462                             |
| Adjustments to reconcile net increase (decrease) in net asset value resulting from operations to net cash used in operating activities: |                                       |                                       |
| Net change in unrealized appreciation or depreciation on investments  | 2,844,314                             | (1,136,098)                           |
| Net realized gain on investments  | (183,416 )                            | (289,439 )                            |
| Payments for purchases of investments   | (3,999,675)                           | (3,683,510)                           |
| Proceeds from sales of investments  | 2,762,478                             | 1,279,857                             |
| Depreciation and amortization   | 12,849                                | 12,658                                |
| Changes in operating assets and liabilities:  |                                       |                                       |
| Receivable from sale on investments   | 82,103                                | (81,309 )                             |
| Interest and dividends receivable   | 35,954                                | (56,044 )                             |
| Prepaid expenses  | 5,815                                 | 4,778                                 |
| Accounts payable  | (25,667 )                             | 17,814                                |
| Deferred rent   | 1,128                                 | 2,246                                 |
| Deferred interest income  | 5,645                                 | —                                     |
| Accrued royalty   | —                                     | (619 )                                |
| Payable for purchase of investment  | 65,622                                | —                                     |
| Net cash used in operating activities   | (1,125,252)                           | (2,963,204)                           |
| Cash flows from investing activities:   |                                       |                                       |
| Purchases of property and equipment   | —                                     | (4,866 )                              |
| Purchases of leasehold improvements   | —                                     | (1,796 )                              |
| Net cash used in investing activities   | —                                     | (6,662 )                              |
| Cash flows from financing activities:   |                                       |                                       |
| Payment for repurchase of common stock  | —                                     | (14,602)                              |
| Net cash used in financing activities   | —                                     | (14,602 )                             |
| Net decrease in cash  | (1,125,252)                           | (2,984,468)                           |
| Cash, beginning of the year   | 4,105,911                             | 7,090,379                             |
| Cash, end of the year   | \$2,980,659                           | \$4,105,911                           |

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

Mill City Ventures III, Ltd.

## Consolidated Financial Highlights

|  | Year<br>Ended<br>31, 2015 | Dec | Year<br>Ended<br>31, 2014 | Dec | Year<br>Ended<br>31, 2013 | Dec |
|--|---------------------------|-----|---------------------------|-----|---------------------------|-----|
| <b>Per Share Data</b>                              |                           |     |                           |     |                           |     |
| Net asset value at beginning of period             | 0.94                      |     | 0.86                      |     | 0.04                      |     |
| Net investment income                              | 0.00                      |     | (0.04                     | )   | (0.05                     | )   |
| Net realized and unrealized losses                 | (0.22                     | )   | 0.12                      |     | 0.03                      |     |
| Issuance of common stock                           | 0.00                      |     | 0.00                      |     | 0.84                      |     |
| Net asset value at end of period                   | 0.72                      |     | 0.94                      |     | 0.86                      |     |
| <b>Ratio / Supplemental Data</b>                   |                           |     |                           |     |                           |     |
| Per share market value at end of period            | 0.47                      |     | 0.59                      |     | 0.27                      |     |
| Shares outstanding at end of period                | 12,151,493                |     | 12,151,493                |     | 12,169,422                |     |
| Average weighted shares outstanding for the period | 12,151,493                |     | 12,166,608                |     | 10,219,737                |     |
| Net assets at end of period                        | 8,741,288                 |     | 11,473,690                |     | 10,521,830                |     |
| Average net assets                                 | 10,520,199                |     | 11,416,452                |     | 8,538,872                 |     |
| Portfolio turnover rate                            | 26.26                     | %   | 11.21                     | %   | 7.53                      | %   |
| Ratio of operating expenses to average net assets  | -6.08                     | %   | -7.00                     | %   | -7.12                     | %   |
| Ratio of net operating loss to average net assets  | -0.68                     | %   | -4.02                     | %   | -6.71                     | %   |
| Ratio of realized gains to average net assets      | 1.74                      | %   | 2.54                      | %   | 1.51                      | %   |

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

Table of Contents 6

**Mill City Ventures III, Ltd**  
**Schedule of Investments**  
**As of December 31, 2015**

| Investments <sup>(1)</sup>       | Investment Type             | Interest Rate <sup>(2)</sup> | Maturity Date | Principal Amount | Cost        | Fair Value  | Percentage of Net Assets | Gross Unrealized Appreciation | Gross Unrealized Depreciation |
|----------------------------------|-----------------------------|------------------------------|---------------|------------------|-------------|-------------|--------------------------|-------------------------------|-------------------------------|
| <b>Debt Investments</b>          |                             |                              |               |                  |             |             |                          |                               |                               |
| <b>Advertising</b>               |                             |                              |               |                  |             |             |                          |                               |                               |
| Creative Realities, Inc.         | Secured Loan <sup>(3)</sup> | 12% cash + 2% pik            | 4/15/2017     | \$600,000        | \$600,000   | \$600,000   | 6.86%                    | —                             | —                             |
| <b>Consumer</b>                  |                             |                              |               |                  |             |             |                          |                               |                               |
| Mix 1 Life, Inc.                 | Secured Loan <sup>(4)</sup> | 12%                          | 2/6/2016      | \$500,000        | 500,000     | 500,000     |                          | —                             | —                             |
| Mix 1 Life, Inc.                 | Secured Loan                | 12%                          | 3/13/2016     | \$250,000        | 250,000     | 250,000     |                          | —                             | —                             |
|                                  |                             |                              |               |                  | 750,000     | 750,000     | 8.58%                    | —                             | —                             |
| <b>Financial</b>                 |                             |                              |               |                  |             |             |                          |                               |                               |
| Bravo Financial LLC              | Secured Loan                | 12%                          | 12/31/2015    | \$500,000        | 500,000     | 500,000     | 5.72%                    | —                             | —                             |
| <b>Leisure &amp; Hospitality</b> |                             |                              |               |                  |             |             |                          |                               |                               |
| The Igloo LLC                    | Secured Loan                | 20%                          | 12/31/2016    | \$500,000        | 500,000     | —           | 0.00%                    | —                             | 500,000                       |
| <b>Oil &amp; Gas</b>             |                             |                              |               |                  |             |             |                          |                               |                               |
| Dala Petroleum, Inc.             | Secured Loan                | 12%                          | 12/22/2016    | \$5,195          | 5,195       | —           |                          | —                             | 5,195                         |
| Pacific Oil & Gas LLC            | Secured Loan                | 12%                          | 12/31/2015    | \$25,000         | 25,000      | —           |                          | —                             | 25,000                        |
|                                  |                             |                              |               |                  | 30,195      | —           | 0.00%                    | —                             | 30,195                        |
| <b>Total Debt Investments</b>    |                             |                              |               |                  | \$2,380,195 | \$1,850,000 | 21.16%                   | —                             | \$530,195                     |

Table of Contents 7

| Investments <sup>(1)</sup> | Investment Type <sup>(5)</sup> | Interest Rate <sup>(6)</sup> | Expiration Date <sup>(7)</sup> | Shares/Units | Cost | Fair Value | Percentage of Net Assets | Gross Unrealized Appreciation | Gross Unrealized Depreciation |
|----------------------------|--------------------------------|------------------------------|--------------------------------|--------------|------|------------|--------------------------|-------------------------------|-------------------------------|
| <b>Equity Investments</b>  |                                |                              |                                |              |      |            |                          |                               |                               |
| <b>Advertising</b>         |                                |                              |                                |              |      |            |                          |                               |                               |
| Creative Realities, Inc.   | Warrants <sup>(8)</sup>        | n/a                          | 12/28/2020                     | 1,071,429    | —    | —          |                          | —                             | —                             |
| Creative Realities, Inc.   | Common Stock <sup>(8)</sup>    | n/a                          | n/a                            | 975,000      | —    | 243,750    |                          | 243,750                       | —                             |
|                            |                                |                              |                                |              | —    | 243,750    | 2.79%                    | 243,750                       | —                             |
| <b>Bio-technology</b>      |                                |                              |                                |              |      |            |                          |                               |                               |
| Bio Life Solutions, Inc.   | Warrants <sup>(8)</sup>        | n/a                          | 3/20/2021                      | 100,000      | —    | —          |                          | —                             | —                             |
| Combimatrix Corporation    | Warrants <sup>(8)</sup>        | n/a                          | 5/6/2019                       | 81,967       | —    | —          |                          | —                             | —                             |
| Combimatrix Corporation    | Warrants <sup>(8)</sup>        | n/a                          | 6/28/2019                      | 81,967       | —    | —          |                          | —                             | —                             |
| Combimatrix Corporation    | Warrants <sup>(8)</sup>        | n/a                          | 12/19/2018                     | 250,000      | —    | —          |                          | —                             | —                             |
|                            |                                |                              |                                |              | —    | —          | 0.00%                    | —                             | —                             |

Table of Contents 8

**Consumer**

|                              |                                     |        |         |         |         |       |         |        |          |
|------------------------------|-------------------------------------|--------|---------|---------|---------|-------|---------|--------|----------|
| Mix 1 Life, Inc.             | Common Stock <sup>(8)</sup>         | n/an/a | 237,470 | —       | 237,470 |       | 237,470 | —      | 237,470  |
| Tzfat Spirits of Israel, LLC | LLC Membership Units <sup>(8)</sup> | n/an/a | 55,000  | 101,019 | 25,000  |       | —       | 76,019 | (76,019) |
|                              |                                     |        |         | 101,019 | 262,470 | 3.00% | 237,470 | 76,019 | 161,451  |

**Financial**

|                       |                             |        |       |        |        |       |   |        |          |
|-----------------------|-----------------------------|--------|-------|--------|--------|-------|---|--------|----------|
| Comm. Sales & Leasing | Common Stock <sup>(9)</sup> | n/an/a | 2,000 | 65,620 | 37,380 | 0.43% | — | 28,240 | (28,240) |
|-----------------------|-----------------------------|--------|-------|--------|--------|-------|---|--------|----------|

**Healthcare**

|                            |                             |        |            |         |         |       |   |        |          |
|----------------------------|-----------------------------|--------|------------|---------|---------|-------|---|--------|----------|
| WaferGen Bio-Systems, Inc. | Common Stock <sup>(8)</sup> | n/an/a | 200,000    | 200,000 | 146,760 |       | — | 53,240 | (53,240) |
| WaferGen Bio-Systems, Inc. | Warrants <sup>(8)</sup>     | n/a    | 10/21/2020 | 200,000 | —       |       | — | —      | —        |
|                            |                             |        |            | 200,000 | 146,760 | 1.68% | — | 53,240 | (53,240) |

**Information Technology**

|                                |                                |        |            |         |         |       |         |   |         |
|--------------------------------|--------------------------------|--------|------------|---------|---------|-------|---------|---|---------|
| Insite Software Solutions, Inc | Warrants <sup>(8)</sup>        | n/a    | 12/30/2023 | 108,960 | —       |       | —       | — | —       |
| MAX 4G                         | Preferred Stock <sup>(8)</sup> | n/an/a | 300,000    | 150,000 | 300,000 |       | 150,000 | — | 150,000 |
| Simulations Plus, Inc.         | Common Stock                   | n/an/a | 5,000      | 47,869  | 49,550  |       | 1,681   | — | 1,681   |
|                                |                                |        |            | 197,869 | 349,550 | 4.00% | 151,681 | — | 151,681 |

**Investment Fund**

|                                 |                             |        |        |         |         |       |   |        |          |
|---------------------------------|-----------------------------|--------|--------|---------|---------|-------|---|--------|----------|
| Calamos Conv. & High Inc. Fund  | Common Stock <sup>(9)</sup> | n/an/a | 10,000 | 128,357 | 105,100 |       | — | 23,257 | (23,257) |
| Powershares High Dividend Yield | Common Stock <sup>(9)</sup> | n/an/a | 10,000 | 253,510 | 210,000 |       | — | 43,510 | (43,510) |
| Solar Senior Capital Ltd        | Common Stock <sup>(9)</sup> | n/an/a | 6,047  | 91,983  | 90,100  |       | — | 1,883  | (1,883)  |
|                                 |                             |        |        | 473,850 | 405,200 | 4.64% | — | 68,650 | (68,650) |

**Leisure & Hospitality**

|                                 |  |        |         |           |           |        |   |   |   |
|---------------------------------|--|--------|---------|-----------|-----------|--------|---|---|---|
| Bitesquad.com LLC               | Preferred LLC Units <sup>(4)(8)</sup>    | n/an/a | 60,000  | 780,000   | 780,000   | 8.92%  | — | — | — |
| DBR Phase III US Investors, LLC | Limited Partnership Units <sup>(8)</sup> | n/an/a | 761,050 | 761,050   | 761,050   | 8.71%  | — | — | — |
|                                 |  |        |         | 1,541,050 | 1,541,050 | 17.63% | — | — | — |

**Media**

|                               |                             |        |       |         |         |       |   |        |          |
|-------------------------------|-----------------------------|--------|-------|---------|---------|-------|---|--------|----------|
| Discovery Communications Inc. | Common Stock <sup>(9)</sup> | n/an/a | 5,000 | 149,609 | 133,400 | 1.53% | — | 16,209 | (16,209) |
|-------------------------------|-----------------------------|--------|-------|---------|---------|-------|---|--------|----------|



**Oil & Gas**

|                                 |  |        |          |           |         |       |         |           |             |
|---------------------------------|--|--------|----------|-----------|---------|-------|---------|-----------|-------------|
| Dala Petroleum, Inc.            | Preferred Stock <sup>(8)</sup>           | n/an/a | 500      | 500,000   | —       | —     | 500,000 | (500,000) |             |
|                                 | Warrants <sup>(8)</sup>                  | n/a    | 6/3/2017 | 714,286   | —       | —     | —       | —         |             |
| Northern Capital Partners I, LP | Limited Partnership Units <sup>(8)</sup> | n/an/a | 500,000  | 500,000   | 444,208 | —     | 55,792  | (55,792)  |             |
| Southern Plains Resources, Inc. | Common Stock <sup>(8)</sup>              | n/an/a | 600,000  | 730,000   | —       | —     | 730,000 | (730,000) |             |
|                                 |  |        |          | 1,730,000 | 444,208 | 5.08% | —       | 1,285,792 | (1,285,792) |

**Publishing**

|                               |              |        |       |        |        |       |     |   |     |
|-------------------------------|--------------|--------|-------|--------|--------|-------|-----|---|-----|
| Educational Development Corp. | Common Stock | n/an/a | 2,300 | 25,212 | 25,461 | 0.29% | 249 | — | 249 |
|-------------------------------|--------------|--------|-------|--------|--------|-------|-----|---|-----|

**Telecommunications**

|                          |                             |        |       |         |         |       |   |        |          |
|--------------------------|-----------------------------|--------|-------|---------|---------|-------|---|--------|----------|
| AT&T                     | Common Stock <sup>(9)</sup> | n/an/a | 5,000 | 175,260 | 172,050 | —     | — | 3,210  | (3,210)  |
| CenturyLink, Inc.        | Common Stock <sup>(9)</sup> | n/an/a | 5,000 | 157,360 | 125,800 | —     | — | 31,560 | (31,560) |
| Windstream Holdings Inc. | Common Stock <sup>(9)</sup> | n/an/a | 1,666 | 21,087  | 10,729  | —     | — | 10,358 | (10,358) |
|                          |                             |        |       | 353,707 | 308,579 | 3.53% | — | 45,128 | (45,128) |

**Total Equity Investments**

\$4,837,936 \$3,897,808 44.59% \$633,150 \$1,573,278 (\$99,000)

**Total Cash**

\$2,980,659 \$2,980,659 34.10% — — —

**Total Investments (10)**

\$10,198,790 \$8,728,467 99.85% \$633,150 \$2,103,473 (\$1,462,163)

(1) All investments and all cash, restricted cash and cash equivalents 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 secured but payment and collateral are subordinated to the debt of another creditor by contract.

(4) Investment is convertible into common equity of the issuer.

(5) In the case of warrants, warrants provide for the right to purchase common equity of the issuer.

(6) In the case of preferred stock, this represents the right to annual cumulative dividends calculated on a per annum basis.

(7) In the case of warrants, purchase rights under the warrants will expire at the close of business on this date.

(8) Investment is not an income-producing investment.

(9) Investment is not a “qualifying asset” under Section 55(a) of the Investment Company Act of 1940.

(10) Investments that are not “qualified assets” under Section 55 of the Investment Company Act of 1940 represent 15.4% of total investments, and 10.0% of total assets.

Table of Contents 10

**Mill City Ventures III, Ltd.**  
**Schedule of Investments**  
**As of December 31, 2014**

| <b>Investments <sup>(1)</sup></b> | <b>Investment Type</b>      | <b>Interest Rate <sup>(2)</sup></b> | <b>Maturity Date</b> | <b>Principal Amount</b> | <b>Cost</b> | <b>Fair Value</b> | <b>Percentage of Net Assets</b> | <b>Gross Unrealized Appreciation</b> | <b>Gross Unrealized Depreciation</b> |   |
|-----------------------------------|-----------------------------|-------------------------------------|----------------------|-------------------------|-------------|-------------------|---------------------------------|--------------------------------------|--------------------------------------|---|
| <b>Debt Investments</b>           |                             |                                     |                      |                         |             |                   |                                 |                                      |                                      |   |
| <b>Consumer</b>                   |                             |                                     |                      |                         |             |                   |                                 |                                      |                                      |   |
| Mix 1 Life, Inc.                  | Secured Loan <sup>(4)</sup> | 12%                                 | 2/6/2016             | \$500,000               | 500,000     | 500,000           | 5.72%                           | —                                    | —                                    |   |
| <b>Information Technology</b>     |                             |                                     |                      |                         |             |                   |                                 |                                      |                                      |   |
| Insite Software Solutions, Inc    | Secured Loan                | 10.5%                               | 12/30/2018           | 750,000                 | 750,000     | 750,000           | 8.58%                           | —                                    | —                                    |   |
| <b>Leisure &amp; Hospitality</b>  |                             |                                     |                      |                         |             |                   |                                 |                                      |                                      |   |
| The Igloo LLC                     | Secured Loan                | 20%                                 | 12/31/2016           | 500,000                 | 500,000     | 500,000           | 5.72%                           | —                                    | —                                    |   |
| <b>Total Debt Investments</b>     |                             |                                     |                      |                         |             | \$1,750,000       | \$1,750,000                     | 20.02%                               | —                                    | — |

Table of Contents 11

| Investments <sup>(1)</sup>      | Investment Type <sup>(5)</sup>      | Interest Rate <sup>(6)</sup> | Expiration Date <sup>(7)</sup> | Shares/Units | Cost    | Fair Value | Percentage of Net Assets | Gross Unrealized Appreciation |
|---------------------------------|-------------------------------------|------------------------------|--------------------------------|--------------|---------|------------|--------------------------|-------------------------------|
| <b>Equity Investments</b>       |                                     |                              |                                |              |         |            |                          |                               |
| <b>Bio-technology</b>           |                                     |                              |                                |              |         |            |                          |                               |
| Bio Life Solutions, Inc.        | Common Stock <sup>(8)</sup>         | n/a                          | n/a                            | 50,000       | 215,000 | 82,000     |                          | —                             |
| Bio Life Solutions, Inc.        | Warrants <sup>(8)</sup>             | n/a                          | 3/20/2021                      | 100,000      | —       | —          |                          | —                             |
| Combimatrix Corporation         | Warrants <sup>(8)</sup>             | n/a                          | 5/6/2019                       | 81,967       | —       | —          |                          | —                             |
| Combimatrix Corporation         | Warrants <sup>(8)</sup>             | n/a                          | 6/28/2019                      | 81,967       | —       | —          |                          | —                             |
| Combimatrix Corporation         | Warrants <sup>(8)</sup>             | n/a                          | 12/19/2018                     | 250,000      | —       | —          |                          | —                             |
|                                 |                                     |                              |                                |              | 215,000 | 82,000     | 0.94%                    | —                             |
| <b>Consumer</b>                 |                                     |                              |                                |              |         |            |                          |                               |
| Mix 1 Life, Inc.                | Common Stock <sup>(8)</sup>         | n/a                          | n/a                            | 352,230      | —       | 1,958,399  |                          | 1,958,399                     |
| Tzfat Spirits of Israel, LLC    | LLC Membership Units <sup>(8)</sup> | n/a                          | n/a                            | 55,000       | 101,019 | 25,000     |                          | —                             |
|                                 |                                     |                              |                                |              | 101,019 | 1,983,399  | 22.69%                   | 1,958,399                     |
| <b>Information Technology</b>   |                                     |                              |                                |              |         |            |                          |                               |
| Insite Software Solutions, Inc  | Warrants <sup>(8)</sup>             | n/a                          | 12/30/2023                     | 108,960      | —       | —          |                          | —                             |
| MAX 4G                          | Preferred Stock <sup>(8)</sup>      | n/a                          | n/a                            | 300,000      | 150,000 | 150,000    |                          | —                             |
|                                 |                                     |                              |                                |              | 150,000 | 150,000    | 1.72%                    | —                             |
| <b>Investment Fund</b>          |                                     |                              |                                |              |         |            |                          |                               |
| Calamos Conv. & High Inc. Fund  | Common Stock <sup>(9)</sup>         | n/a                          | n/a                            | 10,000       | 128,357 | 138,300    |                          | 9,943                         |
| Powershares High Dividend Yield | Common Stock <sup>(9)</sup>         | n/a                          | n/a                            | 10,000       | 253,510 | 252,860    |                          | —                             |
|                                 |                                     |                              |                                |              | 381,867 | 391,160    | 4.47%                    | 9,943                         |

Table of Contents 12

**Leisure & Hospitality**

|                                 |  |        |           |           |           |        |   |   |
|---------------------------------|--|--------|-----------|-----------|-----------|--------|---|---|
| DBR Phase III US Investors, LLC | Limited Partnership Units <sup>(8)</sup> | n/an/a | 1,000,000 | 1,000,000 | 1,000,000 | 11.44% | — | — |
|---------------------------------|--|--------|-----------|-----------|-----------|--------|---|---|

**Oil & Gas**

|                                 |  |        |          |           |           |        |   |         |
|---------------------------------|--|--------|----------|-----------|-----------|--------|---|---------|
| Dala Petroleum, Inc.            | Preferred Stock <sup>(8)</sup>           | n/an/a | 500      | 500,000   | 500,000   | —      | — | —       |
|                                 | Warrants <sup>(8)</sup>                  | n/a    | 6/3/2017 | 14,286    | —         | —      | — | —       |
| Northern Capital Partners I, LP | Limited Partnership Units <sup>(8)</sup> | n/an/a | 500,000  | 500,000   | 500,000   | —      | — | —       |
| Southern Plains Resources, Inc. | Common Stock <sup>(8)</sup>              | n/an/a | 600,000  | 730,000   | 300,000   | —      | — | 430,000 |
|                                 |  |        |          | 1,730,000 | 1,300,000 | 14.87% | — | 430,000 |

**Telecommunications**

|                               |                             |        |        |         |         |       |        |        |
|-------------------------------|-----------------------------|--------|--------|---------|---------|-------|--------|--------|
| AT&T                          | Common Stock <sup>(9)</sup> | n/an/a | 5,000  | 175,260 | 167,950 | —     | —      | 7,310  |
| CenturyLink, Inc.             | Common Stock <sup>(9)</sup> | n/an/a | 5,000  | 157,360 | 197,900 | —     | 40,540 | —      |
| Frontier Communications Corp. | Common Stock <sup>(9)</sup> | n/an/a | 10,000 | 50,305  | 66,700  | —     | 16,395 | —      |
| Windstream Holdings Inc.      | Common Stock <sup>(9)</sup> | n/an/a | 10,000 | 86,707  | 82,400  | —     | —      | 4,307  |
|                               |                             |        |        | 469,632 | 514,950 | 5.89% | 56,935 | 11,617 |

**Total Equity Investments**

|  |  |  |  |             |             |        |             |           |
|--|--|--|--|-------------|-------------|--------|-------------|-----------|
|  |  |  |  | \$4,047,518 | \$5,421,509 | 62.02% | \$2,025,277 | \$651,287 |
|--|--|--|--|-------------|-------------|--------|-------------|-----------|

**Total Cash**

|  |  |  |  |             |             |        |   |   |
|--|--|--|--|-------------|-------------|--------|---|---|
|  |  |  |  | \$4,105,911 | \$4,105,911 | 46.97% | — | — |
|--|--|--|--|-------------|-------------|--------|---|---|

**Total Investments (10)**

|  |  |  |  |             |              |         |             |           |
|--|--|--|--|-------------|--------------|---------|-------------|-----------|
|  |  |  |  | \$9,903,429 | \$11,277,420 | 129.01% | \$2,025,277 | \$651,287 |
|--|--|--|--|-------------|--------------|---------|-------------|-----------|

(1) All investments and all cash, restricted cash and cash equivalents 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) Intentionally omitted.

(4) Investment is convertible into common equity of the issuer.

(5) In the case of warrants, warrants provide for the right to purchase common equity of the issuer.

(6) In the case of preferred stock, this represents the right to annual cumulative dividends calculated on a per annum basis.

(7) In the case of warrants, purchase rights under the warrants will expire at the close of business on this date.

(8) Investment is not an income-producing investment.

(9) Investment is not a “qualifying asset” under Section 55(a) of the Investment Company Act of 1940.

(10) Investments that are not “qualified assets” under Section 55 of the Investment Company Act of 1940 represent 12.6% of total investments, and 7.9% of total assets.

Table of Contents 13

Mill City Ventures III, Ltd.

Notes to Financial Statements

December 31, 2015 and 2014

## **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. Our business from January 10, 2006 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. Our 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.

### *Use of Estimates*

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and 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. Cash on deposit in excess of FDIC coverage is subject to the usual banking risk of funds in excess of those limits.

Table of Contents 14



Mill City Ventures III, Ltd.

Notes to Financial Statements

December 31, 2015 and 2014

**NOTE 1 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (continued)**

***Fair Value of Financial Instruments***

The carrying amounts of certain of the Company's financial instruments, including cash, 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 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 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.

Table of Contents 15

Mill City Ventures III, Ltd.

Notes to Financial Statements

December 31, 2015 and 2014

**NOTE 1 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (continued)**

***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. Currently, two of our five loans are in default. Three of our loans are current in required interest payments. 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 December 31, 2015 and December 31, 2014 were \$5,747,808 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.

**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:

|   | Year Ended<br>December<br>31,<br>2015 | Year Ended<br>December<br>31,<br>2014 |
|---|---------------------------------------|---------------------------------------|
| Numerator: Net Gain (Loss)  | \$(2,732,402 )                        | \$966,462                             |
| Denominator: Weighted-average number of common shares outstanding | 12,151,493                            | 12,166,608                            |
| Basic and diluted net gain (loss) per common share                | \$(0.22 )                             | \$0.08                                |

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

Mill City Ventures III, Ltd.

Notes to Financial Statements

December 31, 2015 and 2014

### **NOTE 3—COMMITMENTS AND CONTINGENCIES**

On June 6, 2013, the Company entered into an agreement to lease approximately 1,917 square feet of commercial space and two parking spots, for a period of 62 months. The leased space became available for occupancy on September 23, 2013. The 62-month lease term began October 1, 2013 and runs through November 30, 2018. The total base rent expense for the year ended December 31, 2015 and December 31, 2014 was \$45,378 and \$45,378, respectively.

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

| Year  | Amount    |
|-------|-----------|
| 2016  | \$46,179  |
| 2017  | 50,311    |
| 2018  | 46,988    |
| TOTAL | \$143,478 |

### **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 December 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.

Table of Contents 17

Mill City Ventures III, Ltd.

Notes to Financial Statements

December 31, 2015 and 2014

**NOTE 5—FAIR VALUE OF INVESTMENTS – (continued)**

***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 the Company has 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.

Table of Contents 18



Mill City Ventures III, Ltd.

Notes to Financial Statements

December 31, 2015 and 2014

**NOTE 5—FAIR VALUE OF INVESTMENTS – (continued)**

The table below presents the balance of assets measured at fair value on a recurring basis by level within the hierarchy:

|  | December 31, 2015 |         |             | Total       |
|--|-------------------|---------|-------------|-------------|
|  | Level 1           | Level 2 | Level 3     |             |
| AT&T                                   | \$172,050         | \$ —    | \$—         | \$172,050   |
| Calamos Convertible & High Income Fund | 105,100           | —       | —           | 105,100     |
| CenturyLink, Inc.                      | 125,800           | —       | —           | 125,800     |
| Communication Sales & Leasing          | 37,380            | —       | —           | 37,380      |
| Discovery Communications Corporation   | 133,400           | —       | —           | 133,400     |
| Educational Development Corp           | 25,461            | —       | —           | 25,461      |
| Mix 1 Life, Inc                        | 237,470           | —       | —           | 237,470     |
| Simulation Plus Inc                    | 49,550            | —       | —           | 49,550      |
| Solar Senior Capital Ltd.              | 90,100            | —       | —           | 90,100      |
| Powershares High Yield Dividend        | 210,000           | —       | —           | 210,000     |
| WaferGen Bio-Systems                   | 146,760           | —       | —           | 146,760     |
| Windstream Holdings Inc.               | 10,729            | —       | —           | 10,729      |
| Bitesquad LLC                          | —                 | —       | 780,000     | 780,000     |
| Bravo Financial LLC                    | —                 | —       | 500,000     | 500,000     |
| MAX 4G                                 | —                 | —       | 300,000     | 300,000     |
| Tzfat Spirits of Israel, LLC           | —                 | —       | 25,000      | 25,000      |
| DBR Phase III US Investors, LLC        | —                 | —       | 761,050     | 761,050     |
| Mix 1 Life, Inc                        | —                 | —       | 500,000     | 500,000     |
| Mix 1 Life, Inc                        | —                 | —       | 250,000     | 250,000     |
| Northern Capital, LP                   | —                 | —       | 444,208     | 444,208     |
| Creative Realities                     | 243,750           | —       | —           | 243,750     |
| Creative Realities                     | —                 | —       | 600,000     | 600,000     |
| Total                                  | \$1,587,550       | \$ —    | \$4,160,258 | \$5,747,808 |

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

|  | Fair<br>Value |
|--|---------------|
| Fair Value, December 31, 2014  | \$4,225,000   |
| Change in unrealized appreciation  | (1,235,987)   |
| Net realized and unrealized gain   | (1,235,987)   |
| Purchases of portfolio investments   | 3,165,195     |
| Sales of portfolio investments   | (1,988,950)   |
| Fair Value, December 31, 2015  | \$4,160,258   |
| Net unrealized gains included in the<br>net increase in net assets resulting<br>from operations relating to assets<br>held at<br>December 31, 2015 | \$(1,235,987) |

Table of Contents 19

Mill City Ventures III, Ltd.

Notes to Financial Statements

December 31, 2015 and 2014

**NOTE 5—FAIR VALUE OF INVESTMENTS – (continued)**

*Portfolio Investments*

At December 31, 2015, we held investments in 18 eligible portfolio investments, which had an amortized cost of \$6,175,345 and a fair value of \$4,863,249. 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. (“Southern Plains”) 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 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 December 31, 2015 was \$730,000 and the fair value was \$0.

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 warrants to purchase up to 81,967 common shares at 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 warrants to purchase up to 81,967 common shares at 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 up to 250,000 shares of common stock at an exercise price of \$3.12 per share. 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 per share and the 81,967 warrants at \$3.55 to a \$1.97 per share 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 December 31, 2015 the cost and fair value of the warrants was \$0.

Table of Contents 20

Mill City Ventures III, Ltd.

Notes to Financial Statements

December 31, 2015 and 2014

**NOTE 5—FAIR VALUE OF INVESTMENTS – (continued)**

On May 29, 2013, we entered into a subscription and investment letter with MAX4G, Inc. (“MAX4G”) 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 December 31, 2015, the cost of the MAX4G investment was \$150,000 and the fair value was \$300,000.

On October 14, 2013, we entered into subscription agreement with Tzfat Spirits of Israel, LLC (“Tzfat”), to purchase 55,000 Class A Membership Units at \$1.8367 per unit for a total of \$101,019. At December 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. (“Insite Software”) 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 \$0.01 per share. The warrant has a 10-year term expiring December 30, 2023. On April 27, 2015, we received the principal amount of \$750,000 plus \$5,825.34 in accrued interest in full on redemption of the promissory note. At December 31, 2015, the cost and fair value of 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. (“Mix 1 Life”) 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 had 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 December 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 \$237,470, respectively. Our former director, Christopher Larson, is currently the Chief Financial Officer and a director of Mix 1 Life as well as a 5% shareholder. Mr. Larson was appointed the Chief Financial Officer and a director of Mix 1 Life on June 24, 2014, after our initial investment in Mix 1 Life.

## Edgar Filing: Mill City Ventures III, Ltd - Form 10-K/A

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. We funded a second capital call of \$350,000 on May 9, 2014 and a final capital call on October 21, 2014 in the amount of \$300,000. On December 3, 2015, we received \$238,950 payment on the note plus \$90,389 accrued interest. At December 31, 2015, the cost and fair value of the interests was \$761,050.

On June 3, 2014, we entered into a subscription and warrant purchase agreement with Dala Petroleum Corporation (fka Westcott Products Corporation) (“Dala Petroleum”) 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 an exercise price of \$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. On May 25, 2015, we entered into an agreement to defer the receipt of the quarterly dividend distribution on the preferred shares until October 1, 2015. The company did not make the prescribed payment and has subsequently notified us of its inability to make the payment. The deferred dividend of \$7,500 for each of the quarters ended June 30, September 30, and December 31, 2015 was deemed uncollectible and removed from Dividend Income on the Statement of Operations as of December 31, 2015. At December 31, 2015, the cost and fair value of the preferred stock was \$500,000 and \$0, respectively, and the cost and fair value of the warrant was \$0. Other holders of Dala Petroleum’s preferred stock have proposed a plan for additional funding for the company and reducing the conversion price of the preferred stock and associated warrants. There can be no assurance the plan for additional funding will be agreed upon by all preferred holders or that any additional financings would have a beneficial effect on Dala Petroleum’s operations or future prospects.

Table of Contents 21

Mill City Ventures III, Ltd.

Notes to Financial Statements

December 31, 2015 and 2014

**NOTE 5—FAIR VALUE OF INVESTMENTS – (continued)**

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, 2014. We funded a second capital call of \$125,000 on August 26, 2014, a third capital call of \$200,000 on October 21, 2014 and the fourth and final capital call of \$125,000 on December 26, 2014. At December 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 (“The Igloo”) and in connection therewith funded a \$500,000 promissory note. At December 31, 2015, the cost and fair value of the note was \$500,000 and \$0, respectively. The Igloo no longer operates the facility and has been blocked by the landlord, who has filed a lawsuit seeking monetary damages under The Igloo’s lease agreement. As of December 31, 2015, we were pursuing our rights under the note agreement with respect to a claim on certain collateral.

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 per share. In conjunction with the financing, we received a warrant to purchase up to 1,515,152 common shares at a conversion price of \$0.38 per share. The warrant has a cashless conversion provision and expires February 17, 2020. On October 14, 2015 we received the principal amount of \$1,000,000 plus \$46,684.93 in accrued interest in full on redemption of the promissory note. On December 28, 2015, the warrants were exchanged for zero cost into 975,000 shares of common stock. At December 31, 2015, the cost and fair value of the common stock was \$0 and \$243,750, respectively..

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

On June 1, 2015, we purchased a 12% promissory note from Pacific Oil & Gas, LLC (“POG”) for \$25,000 principal amount. The note plus accrued interest is due on December 31, 2015. At December 31, 2015, the cost and fair value of the note was \$25,000 and \$0, respectively. POG is a related entity to Dala Petroleum, another portfolio company, and

has not been successful in deploying capital with the intended result of successful oil production. We believe due to financial constraints POG will not be able to meet its financial obligations to us.

On August 31, 2015, we entered into a promissory note agreement with Bravo Financial, LLC for \$1,000,000 principal amount. A first advance in the amount of \$500,000 was therein funded on September 1, 2015. The note bears 12% annual interest paid monthly in arrears and is due August 31, 2018. At December 31, 2015, the cost and fair value of the note was \$500,000.

On September 21, 2015, we entered into purchase agreement with Bite Squad, LLC to purchase 60,000 shares of Series A Convertible Preferred Stock at \$13 per share, for a total of \$780,000. The preferred stock converts to common at \$13 per share. At December 31, 2015, the cost and fair value of the preferred stock was \$780,000.

On October 21, 2015, we purchased 200,000 shares of Common Stock of WaferGen Bio-Systems Inc. at \$1 per share, for a total of \$200,000. We also received 200,000 warrants which convert to common at \$1.44 per share and expire October 21, 2020. At December 31, 2015, the cost of the common stock was \$200,000 and fair value was \$146,760, and the cost and fair value of the warrant was \$0.

Table of Contents 22



Mill City Ventures III, Ltd.

Notes to Financial Statements

December 31, 2015 and 2014

**NOTE 5—FAIR VALUE OF INVESTMENTS – (continued)**

On December 24, 2015, we purchased 804 shares of Common Stock of Simulations Plus Inc. at \$9.25 per share, for a total of \$7,759. On December 29 we added 1,996 shares to our holdings at \$9.60 per share for a total of \$19,224. On December 30 we added 2,200 shares to our holdings at \$9.60 per share for a total of \$21,186, bringing our total holdings to 5,000 shares at December 31, 2015. At December 31, 2015, the cost and fair value of the common stock was \$47,869 and \$49,550, respectively.

On December 31, 2015, we purchased 2,300 shares of Common Stock of Educational Development Corporation at \$10.93 per share, for a total of \$25,212. At December 31, 2015, the cost and fair value of the common stock was \$25,212 and \$25,461, respectively.

On December 28, 2015, we purchased a 14% convertible note from Creative Realities, Inc. for \$600,000 principal amount. The note bears 12% annual interest paid monthly in arrears plus 2% annual interest payable in additional principal at the term of the note. The note is due April 15, 2017. The outstanding principal amount is convertible into common stock at \$0.28 per share. In conjunction with the financing, we received a warrant to purchase up to 1,071,429 common shares at a conversion price of \$0.28 per share. The warrant has a cashless conversion provision and expires December 28, 2020. At December 31, 2015, the cost and fair value of the convertible note was \$600,000.

**NOTE 6—MINIMUM ASSET COVERAGE**

As a BDC, we are required to meet various regulatory 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 December 31, 2015, approximately 85% 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. Once we have elected RIC status, we will be 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. The character 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. The Company did not have any taxable income for the year ended December 31, 2015.

#### **NOTE 8—SUBSEQUENT EVENTS**

On March 17, 2016, the Company entered into a Settlement and Forbearance Agreement involving Christopher M. Gentz, Jr., the guarantor of the \$500,000 debt owed by The Igloo, LLC to the Company. The terms of the agreement provide that the Company forbears from commencing or continuing legal action to recover such debt until August 1, 2016, unless a forbearance event of defaults occurs under the agreement and contemplates the assignment of the Company’s rights claims and interests against Mr Gnetz and The Igloo LLC to a third party in consideration for payments as follows: (i) \$15,000 by March 31, 2016; (ii) \$50,000 by May 1, 2016; and (iii) \$70,000 by August 1, 2016. The settlement payments will be recorded upon receipt of cash due to the uncertainty of receipt.

Table of Contents 23

Mill City Ventures III, Ltd.

Notes to Financial Statements

December 31, 2015 and 2014

**NOTE 8—SUBSEQUENT EVENTS – (continued)**

On January 22, 2016, we received \$434,195 from DBR Phase III US Investors, LLC. The payment represented a \$418,750 principal payment on the note plus \$15,445 accrued interest. On March 22, we received a final principal payment from DBR for \$342,300 and accrued interest of \$6,316. The note and accrued interest have now been paid in full.

We have agreed in principal to extend both notes (\$500,000 and \$250,000) owed by Mix 1 Life, Inc. We have received accrued and 30 day forward interest on these notes and are finalizing an extension agreement.

Table of Contents 24

## SIGNATURES

In accordance with the requirements of the Securities Exchange Act of 1934, the registrant has 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: August 15, 2016

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

| <b>Signature and Name</b>                        | <b>Position/Title</b>  | <b>Date</b>     |
|--|--|-----------------|
| /s/ Douglas M. Polinsky<br>Douglas M. Polinsky   | Chief Executive Officer, President and<br>Director (principal executive officer)     | August 15, 2016 |
| /s/ Joseph A. Geraci, II<br>Joseph A. Geraci, II | Chief Financial Officer and Director<br>(principal accounting and financial officer) | August 15, 2016 |
| /s/ Lyle Berman<br>Lyle Berman                   | Director   | August 15, 2016 |
| /s/ Howard Liszt<br>Howard Liszt                 | Director   | August 15, 2016 |
| /s/ Laurence Zipkin<br>Laurence S. Zipkin        | Director   | August 15, 2016 |

Table of Contents 25

