Harvest Capital Credit Corp
Form 10-Q
June 11, 2013

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2013

OR

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

COMMISSION FILE NUMBER: 1-35906

HARVEST CAPITAL CREDIT CORPORATION

(Exact Name of Registrant as Specified in Its Charter)

Delaware	**46-1396995**
(State or other Jurisdiction of Incorporation or Organization)	**(I.R.S. Employer Identification No.)**

450 Park Avenue, Suite 500
New York, NY 10022

(Address of Principal Executive Offices) (Zip Code)

(212) 906-3500

(Registrant’s Telephone Number, Including Area Code)

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

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

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

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

The number of shares of the registrant's Common Stock, $0.001 par value, outstanding as of June 7, 2013 was 6,081,132.

HARVEST CAPITAL CREDIT CORPORATION

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PART I—FINANCIAL INFORMATION

Item 1. Financial Statements

Harvest Capital Credit LLC

Statement of Assets and Liabilities

	March 31, 2013 (unaudited)		December 31, 2012	
ASSETS:				
Investments, at fair value:				
Affiliate investments (cost of $1,537,655 and $1,514,642, respectively)	$	1,537,655	$	1,514,642
Non-control/non-affiliate investments (cost of $38,420,948 and $37,092,784, respectively)		38,837,769		37,419,638
Equity/warrants in affiliate investments (cost of $401,514 and $401,514, respectively)		259,360		401,514
Equity/warrants in non-control/non-affiliate investments (cost of $644,774 and $544,774, respectively)		2,843,024		2,175,524
Total investments at fair value (cost of $41,004,891 and $39,553,714, respectively)		43,477,808		41,511,318
Cash		528,735		7,639,801
Interest receivable		355,090		166,592
Deferred financing costs		171,135		180,786
Other assets		348,338		246,541
Total assets	$	44,881,106	$	49,745,038
LIABILITIES:				
Revolving line of credit - related party	$	22,226,666	$	28,226,666
Accrued interest payable - related party		460,557		304,293
Accounts payable and accrued expenses		1,747,159		1,231,006
Other liabilities		15,596		15,971
Total liabilities		24,449,978		29,777,936
Commitments and contingencies (Note 9)				

Mezzanine equity		160,775		160,775
NET ASSETS:				
Common stock, 10,000,000 shares authorized, and 1,172,688 and 1,172,688 issued and outstanding, respectively		17,266,955		17,266,955
Capital in excess of common stock		203,389		254,677
Net realized gains on investments		327,091		327,091
Net unrealized appreciation on investments		2,472,918		1,957,604
Total net assets		20,270,353		19,806,327
Total liabilities and net assets	$	44,881,106	$	49,745,038
Common stock issued and outstanding (1)		1,172,688		1,172,688
Net asset value per common share	$	17.29	$	16.89

(1) Adjusted for the conversion rate of 0.9913 shares for each unit. See Note 1.

See Notes to Unaudited Financial Statements.

Harvest Capital Credit LLC

Statements of Operations (unaudited)

	Three Months Ended March 31, 2013	Three Months Ended March 31, 2012
Investment Income:		
Interest:		
Cash - affiliate investments	$54,150	$-
Cash - non-control/non-affiliate investments	1,337,629	418,733
PIK - affiliate investments	14,012	-
PIK - non-control/non-affiliate investments	268,419	64,761
Fee amortization, net	111,875	16,544
Total interest income	1,786,085	500,038
Other income	-	26,500
Total investment income	**1,786,085**	**526,538**
Expenses:		
Interest expense - revolving line of credit	457,977	140,864
Interest expense - unused line of credit	8,877	22,717
Interest expense - deferred financing costs	9,651	8,853
Total interest expense	476,505	172,434
General and administrative	97,223	42,076
Base management fees	77,351	24,811
Incentive management fees	320,063	65,846
Administrative services expense	50,001	15,000
Total expenses	**1,021,143**	**320,167**
Net investment income	**764,942**	**206,371**
Net change in unrealized appreciation on investments	515,313	57,014
Total net realized and unrealized gains on investments	**515,313**	**57,014**
Net increase in net assets resulting from operations	**$1,280,255**	**$263,385**
Net increase in net assets resulting from operations per share (basic and diluted) (1)	$1.09	$0.55
Weighted average shares outstanding (basic and diluted) (1)	1,172,688	475,518

(1) Adjusted for the conversion rate of 0.9913 shares for each unit. See Note 1.

See Notes to Unaudited Financial Statements.

Harvest Capital Credit LLC

Statements of Changes in Net Assets (unaudited)

	Three Months Ended March 31, 2013	**Three Months Ended March 31, 2012**
Increase in net assets from operations:		
Net investment income	$764,942	$206,371
Net change in unrealized appreciation on investments	515,313	57,014
Net increase in net assets resulting from operations	1,280,255	263,385
Distributions to equity holders (1)	(816,229)	(184,999)
Capital share transactions:		
Issuance of common shares (net of offering costs and sales commissions of $15,509 and $44,820, respectively for 2012)	-	4,565,693
Net increase in net assets from capital share transactions	-	4,565,693
Total increase in net assets	464,026	4,644,079
Net assets at beginning of period	19,806,327	5,708,063
Net assets at end of period	$20,270,353	$10,352,142
Capital share activity (common shares):		
Shares sold (2)	-	312,130
Net increase in capital share activity (common shares)	-	312,130
Capital share activity (mezzanine equity):		
Shares sold (2)	-	2,478
Net increase in capital share activity (mezzanine equity)	-	2,478

(1) The distribution made in Q1 2013 was for Q4 2012 earnings. This distribution was comprised of $649,845 from net investment income and $166,384 from realized gains.

(2) Adjusted for the conversion rate of 0.9913 shares for each unit. See Note 1.

See Notes to Unaudited Financial Statements.

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Harvest Capital Credit LLC

Statements of Cash Flows (unaudited)

	Three Months Ended March 31, 2013	**Three Months Ended March 31, 2012**
Cash flows from operating activities:		
Net increase in net assets resulting from operations	$1,280,255	$263,385
Adjustments to reconcile net increase in net assets resulting from operations to net cash (used) provided by operating activities:		
Paid in kind income	(282,431)	(64,761)
Net unrealized appreciation of investments	(515,313)	(57,014)
Accretion of deferred loan fees	(111,875)	(16,544)
Purchase of investments	(1,100,000)	(6,185,625)
Proceeds from principal payments	43,128	-
Changes in operating assets and liabilities		
Amortization of deferred debt issuance costs	9,651	8,853
Increase in interest receivable	(188,498)	(22,852)
Increase in other assets	(101,797)	(3,559)
Increase in accrued interest payable	156,264	63,503
Increase in accounts payable and other liabilities	515,779	95,052
Net cash used in operating activities	(294,837)	(5,919,562)
Cash flows from financing activities:		
Borrowings on revolving credit facility	1,000,000	3,050,000
Repayment of borrowings on revolving credit facility	(7,000,000)	-
Contributions of equity	-	4,581,202
Issuance of mezzanine equity	-	36,375
Return of capital	-	(91,545)
Distributions to equity holders	(816,229)	-
Payment of deferred financing costs	-	(6,232)
Net cash (used in) provided by financing activities	(6,816,229)	7,569,800
Net increase (decrease) in cash during the period	(7,111,066)	1,650,238
Cash at beginning of period	7,639,801	2,756,475
Cash at end of period	$528,735	$4,406,713

Supplemental disclosures of cash flow information:		
Cash paid during the period for interest	$310,590	$100,078
Non-cash financing activities:		
Distributions declared to equity holders	$-	$184,999

See Notes to Unaudited Financial Statements.

Harvest Capital Credit LLC

Schedule of Investments (unaudited)

March 31, 2013

Portfolio Company	Investment (1)	Origination Date	Outstanding Principal	Cost	Fair Value
Investments in Affiliated Portfolio Companies					
Seafood Product Preparation and Packaging					
Solex (8.9%)*	Senior Secured Term Loan, due 12/28/2016 (15.79%; LIBOR + 12.50% Cash/3.29% PIK)	12/31/2012	$1,714,168	$1,537,655	$1,537,655
	Common Equity (6.34% of fully diluted common equity)			250,000	129,069
	Common Equity Warrants (6.4% of fully diluted common equity)			151,514	130,291
Total Investments in Affiliated Portfolio Companies				**$1,939,169**	**$1,797,015**
Investments in Non-controlled, Non-affiliated Portfolio Companies					
Hand Tool Manufacturing					
Rostra Tool Company (22.9%)*	Junior Secured Subordinated Debt, due 12/15/2014 (Greater of 17.00%; 13.00% Cash/4.00% PIK or LIBOR + 13.50% LIBOR + 9.50% Cash/4.00% PIK)	2/1/2012	4,585,522	4,508,435	4,508,435
	Common Equity Warrants (14.99% of fully diluted common equity)			-	135,000

Heavy and Civil Engineering and Construction					
LNB Construction, Inc. (26.2%)*	Junior Secured Subordinated Debt, due 11/30/2014 (20.00%; 17.00% Cash/3.00% PIK)	8/21/2012	3,427,676	3,214,970	3,214,970
	Options to Purchase Common Equity (16.5% of fully diluted common equity)			193,750	2,091,000
Industrial Fluid Filtration Services					
CRS Reprocessing, LLC (14.7%)*	Senior Secured Term Loan, due 11/02/2015 (15.00%, 12.00% Cash/3.00% PIK)	11/1/2012	3,037,871	2,984,478	2,984,478
Industrial Machinery Manufacturing					
Douglas Machines Corp. (21.0%)*	Junior Secured Subordinated Debt, due 4/6/2017 (16.00%; 12.50% Cash/3.50% PIK)	4/6/2012	4,145,994	4,037,794	4,145,994
	Common Equity Warrants (2.0% of fully diluted common equity)			12,500	115,500
Motor Vehicle Metal Stamping					
JD Norman Industries, Inc (20.6%)* (2)	Junior Secured Subordinated Debt, due 10/31/16 (19.00%; 12.50% Cash/6.50% PIK)	11/3/2011	4,236,117	4,176,632	4,176,632
Novelty Shops					
Peekay Acquisition, LLC (Christals) (8.9%)*	Senior Secured Term Loan, due 12/27/2015 (18.00%; 15.00% Cash/3.00% Accommodation Fee)	12/31/2012	2,000,000	1,696,926	1,696,926
	Common Equity Warrants (Christals Acquisition, LLC) (2.0% of fully diluted common equity)			35,000	35,000
	Common Equity Warrants (Christals Parent, LLC) (8.0% of fully diluted common equity)			70,000	70,000
Other Nondepository Credit Intermediation					

WBL SPE I, LLC (9.8%)*	Senior Secured Term Loan, due 12/28/2015 (18.00% Cash)	12/28/2012	2,000,000	1,943,712	1,980,000
Pawn Retail Outlets					
Pawn Plus, Inc. (18.7%)*	Senior Secured Term Loan, due 12/31/2016 (Greater of 17.00%; 15.00% Cash/2.00% PIK or LIBOR + 14.50%; LIBOR + 12.50% Cash/2.00% PIK)	12/31/2012	3,919,717	3,660,210	3,660,210
	Common Equity Warrants (3.9% of fully diluted common equity)			133,524	133,524
Pharmaceutical Merchant Wholesaler					
Insight Pharmaceuticals, LLC (7.7%)*	Junior Secured Term Loan, due 08/25/2017 (13.25%; LIBOR + 11.75% with 1.50% LIBOR floor)	9/14/2011	1,544,828	1,533,569	1,560,276
Safety Consulting Services					
Safety Services Acquisition Corp. (27.8%)*	Junior Secured Subordinated Debt, due 7/5/2017 (15.0%; 12.50% Cash/2.50% PIK)	4/5/2012	5,466,954	5,389,827	5,466,954
	Preferred Equity (0.65% of fully diluted common equity)			100,000	163,000
Software Publishing					
Blackboard Inc. (9.8%)*	Junior Secured Term Loan, due 04/04/2019 (11.50%; LIBOR + 10.00% with 1.50% LIBOR floor)	11/8/2011	2,000,000	1,824,001	1,992,500
Optimal Blue (17.5%)*	Junior Secured Subordinated Debt, due 03/28/2018 (14.50%; 12.50% Cash/2.00% PIK)	12/28/2012	3,518,278	3,450,394	3,450,394
	Common Equity			100,000	100,000

	(0.38% of fully diluted common equity)		
Total Investments in Non-controlled, Non-affiliated Portfolio Companies		**$39,065,722**	**$41,680,793**
Total Investments as of March 31, 2013 (214.5%)*		**$41,004,891**	**$43,477,808**

* Value as a percent of net assets

(1) All debt investments are income producing. Common equity and all warrants are non-income producing. All of our investments other than LNB Construction, Inc., are qualifying assets for purposes of Section 55(a) of the 1940 Act.

(2) JD Norman was in default of financial covenants as of March 31, 2013 resulting in the accrual of interest at the default rate, which is presented above. The non-default interest rate is 16.00% (12.50% Cash / 3.50% PIK). As of March 31, 2013, however, the company was performing and was held on accrual status.

See Notes to Unaudited Financial Statements.

Harvest Capital Credit LLC

Schedule of Investments

December 31, 2012

Portfolio Company	Investment (1)	Origination Date	Outstanding Principal	Cost	Fair Value
Investments in Affiliated Portfolio Companies					
Seafood Product Preparation and Packaging					
Solex (9.7%)*	Senior Secured Term Loan, due 12/28/2016 (15.79%; LIBOR + 12.50% Cash/3.29% PIK)	12/31/2012	$1,700,000	$1,514,642	$1,514,642
	Common Equity (6.34% of fully diluted common equity)			250,000	250,000
	Common Equity Warrants (6.4% of fully diluted common equity)			151,514	151,514
Total Investments in Affiliated Portfolio Companies				**$1,916,156**	**$1,916,156**
Investments in Non-controlled, Non-affiliated Portfolio Companies					
Hand Tool Manufacturing					
Rostra Tool Company (23.8%)*	Junior Secured Subordinated Debt, due 12/15/2014 (Greater of 17.00%; 13.00% Cash/4.00% PIK or LIBOR + 13.50% LIBOR + 9.50% Cash/4.00% PIK)	2/1/2012	4,540,116	4,454,880	4,454,880
	Common Equity Warrants (14.99% of fully diluted common equity)			-	268,000
Heavy and Civil Engineering and Construction					

LNB Construction, Inc. (23.4%)*	Junior Secured Subordinated Debt, due 11/30/2014 (20.00%; 17.00% Cash/3.00% PIK)	8/21/2012	3,436,199	3,196,867	3,196,867
	Options to Purchase Common Equity (16.5% of fully diluted common equity)			193,750	1,434,000
Industrial Fluid Filtration Services					
CRS Reprocessing, LLC (14.9%)*	Senior Secured Term Loan, due 11/02/2015 (15.00%, 12.00% Cash/3.00% PIK)	11/1/2012	3,015,251	2,957,624	2,957,624
Industrial Machinery Manufacturing					
Douglas Machines Corp. (21.3%)*	Junior Secured Subordinated Debt, due 4/6/2017 (16.00%; 12.50% Cash/3.50% PIK)	4/6/2012	4,110,032	3,997,810	4,110,032
	Common Equity Warrants (2.0% of fully diluted common equity)			12,500	104,000
Motor Vehicle Metal Stamping					
JD Norman Industries, Inc (20.7%)* (2)	Junior Secured Subordinated Debt, due 10/31/16 (19.00%; 12.50% Cash/6.50% PIK)	11/3/2011	4,168,369	4,100,488	4,100,488
Novelty Shops					
Peekay Acquisition, LLC (Christals) (9.0%)*	Senior Secured Term Loan, due 12/27/2015 (18.00%; 15.00% Cash/3.00% Accommodation Fee)	12/31/2012	2,000,000	1,678,500	1,678,500
	Common Equity Warrants (Christals Acquisition, LLC) (2.0% of fully diluted common equity)			35,000	35,000
	Common Equity Warrants (Christals Parent, LLC) (8.0% of fully diluted common equity)			70,000	70,000
Other Nondepository Credit Intermediation					
		12/28/2012	1,000,000	940,000	940,000

WBL SPE I, LLC (4.7%)*	Senior Secured Term Loan, due 12/28/2015 (18.00% Cash)				
Pawn Retail Outlets					
Pawn Plus, Inc. (19.0%)*	Senior Secured Term Loan, due 12/31/2016 (Greater of 17.00%; 15.00% Cash/2.00% PIK or LIBOR + 14.50%; LIBOR + 12.50% Cash/2.00% PIK)	12/31/2012	3,900,000	3,630,193	3,630,193
	Common Equity Warrants (3.9% of fully diluted common equity)			133,524	133,524
Pharmaceutical Merchant Wholesaler					
Insight Pharmaceuticals, LLC (7.9%)*	Junior Secured Term Loan, due 08/25/2017 (13.25%; LIBOR + 11.75% with 1.50% LIBOR floor)	9/14/2011	1,544,828	1,533,109	1,560,276
Safety Consulting Services					
Safety Services Acquisition Corp. (28.1%)*	Junior Secured Subordinated Debt, due 7/5/2017 (15.0%; 12.50% Cash/2.50% PIK)	4/5/2012	5,433,000	5,353,111	5,433,000
	Preferred Equity (0.65% of fully diluted common equity)			100,000	131,000
Software Publishing					
Blackboard Inc. (9.7%)*	Junior Secured Term Loan, due 04/04/2019 (11.50%; LIBOR + 10.00% with 1.50% LIBOR floor)	11/8/2011	2,000,000	1,819,424	1,927,000
Optimal Blue (17.3%)*	Junior Secured Subordinated Debt, due 03/28/2018 (14.50%; 12.50% Cash/2.00% PIK)	12/28/2012	3,500,000	3,430,778	3,430,778
Total Investments in Non-controlled, Non-affiliated Portfolio Companies				**37,637,558**	**39,595,162**

Total Investments as of December 31, 2012 (209.6%)*	**$39,553,714**	**$41,511,318**

* Value as a percent of net assets

(1) All debt investments are income producing. Common equity and all warrants are non-income producing. All of our investments other than LNB Construction, Inc., are qualifying assets for purposes of Section 55(a) of the 1940 Act.

(2) JD Norman was in default of financial covenants as of December 31, 2012 resulting in the accrual of interest at the default rate, which is presented above. The non-default interest rate is 16.00% (12.50% Cash / 3.50% PIK). As of December 31, 2012, however, the company was performing and was held on accrual status.

See Notes to Unaudited Financial Statements.

Harvest Capital Credit LLC

Notes to Unaudited Financial Statements

Note 1. Organization

Harvest Capital Credit Corporation (“HCAP”) was incorporated as a Delaware corporation on November 14, 2012, for the purpose of, among other things, acquiring Harvest Capital Credit LLC (“HCC LLC”). HCAP is an externally managed, closed end, non-diversified management investment company that has filed an election to be treated as a business development company (“BDC”) under the Investment Company Act of 1940, as amended (the “1940 Act”). In addition, for tax purposes, HCAP intends to elect to be treated as a regulated investment company (“RIC”) under Subchapter M of the Internal Revenue Code of 1986, as amended (the “Code”).

On May 2, 2013, HCAP acquired HCC LLC. HCC LLC was organized as a limited liability company in the state of Delaware on February 7, 2011, and commenced operations on September 6, 2011, as an externally-managed specialty finance company with the objective of generating both current income and capital appreciation primarily by making direct investments in the form of subordinated debt and, to a lesser extent, senior debt and minority equity investments in privately-held U.S. small to mid-size companies. Pursuant to the acquisition agreement, immediately prior to HCAP's election to be treated as a BDC under the 1940 Act, the following formation transaction was consummated:

> HCAP acquired HCC LLC through a merger (the “Merger”) with and into HCAP, and the holders of membership interests in HCC LLC received shares of HCAP common stock in exchange for their interests in HCC LLC. As a result of the Merger, the outstanding limited liability company interests in HCC LLC were converted into a number of shares of HCAP common stock equal to (i) $33.7 million (*i.e.*, the net asset value of HCC LLC as of December 31, 2012), plus the proceeds of sales of membership interests by HCC LLC since December 31, 2012, plus the reclassification of mezzanine equity to members capital, and minus distributions of pre-December 31, 2012 earnings made by HCC LLC after December 31, 2012, divided by (ii) $15.00 per share of the common stock of HCAP. In connection with the merger, the number of membership interests of HCC LLC underlying each outstanding warrant of HCC LLC, and the exercise price thereof, were converted into HCAP's common stock equivalent (based on the merger conversion formula). In addition, the exercise prices of the warrants were subject to upward (but not downward) adjustment as the public offering price was higher than the then-current exercise price of the warrants.

HCAP assumed and succeeded to all of the assets and liabilities of HCC LLC, including its obligations under the revolving credit facility with JMP Group LLC.

On May 7, 2013, HCAP closed its initial public offering (“IPO”) of 3,400,000 shares of its common stock at a price of $15.00 per share raising $51.0 million in gross proceeds, or $50.4 million after deducting underwriting discounts and commissions.

On May 17, 2013, HCAP closed on the IPO underwriters’ overallotment option of 433,333 shares of its common stock at $15.00 per share raising additional gross proceeds of $6.5 million, or $6.1 million after deducting underwriting discounts and commissions.

Since HCAP acquired all of the interests of HCC LLC and did not have any operations prior to the acquisition, we are presenting the historical financial statements of HCC LLC as HCAP's financial statements. When HCAP acquired HCC LLC, HCAP issued shares of its common stock in exchange for all HCC LLC's outstanding membership interests at a rate of 0.9913 shares for each membership interest. As a result of this transaction, we have retroactively applied the aforementioned exchange/conversion rate to all unit measurements relating to HCC LLC's membership interests for all periods presented and have replaced all references to membership interests of HCC LLC to shares of common stock of HCAP in the financial statements and notes thereto contained herein. On the date of the Merger, the net asset value of the Company was $15.00 per share and none of the warrants assumed in the Merger had an exercise price below $15.00 per share. As the warrants did not have a dilutive effect on the shares outstanding on the date of the Merger, we are presenting the basic and diluted shares outstanding as the same in the financial statements and notes contained herein.

As used herein, the terms “we”, “us” and the “Company” refer to HCC LLC for the periods prior to the IPO and refer to HCAP for the periods after the IPO.

Note 2. Summary of Significant Accounting Policies

Basis of Financial Statement Presentation

The accompanying interim financial statements are presented in conformity with U.S. generally accepted accounting principles (“U.S. GAAP”) for interim financial information, and pursuant to the requirements for reporting on Form 10-Q and Article 10 of Regulation S-X. Accordingly, certain disclosures accompanying annual financial statements prepared in accordance with U.S. GAAP are omitted. In the opinion of management, all adjustments consisting solely of normal recurring accruals considered necessary for the fair presentation of consolidated financial statements for the interim periods have been included. The interim unaudited financial statements and notes should be read in conjunction with the audited financial statements and notes thereto for the period ended December 31, 2012. Financial statements prepared on a U.S. GAAP basis require management to make estimates and assumptions that affect the amounts and disclosures reported in the financial statements and accompanying notes. Such estimates and assumptions could change in the future as more information becomes known, which could impact the amounts reported and disclosed herein.

Basis for Consolidation

In accordance with Article 6 of Regulation S-X, the Company does not consolidate portfolio company investments.

Under the investment company rules and regulations pursuant to the American Institute of Certified Public Accountants Audit and Accounting Guide for Investment Companies, codified in Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") 946, *Financial Services- Investment Companies*, the Company is precluded from consolidating any entity other than another investment company, except that ASC 946 provides for the consolidation of a controlled operating company that provides substantially all of its services to the investment company or its consolidated subsidiaries.

Cash and Cash Equivalents

Cash and cash equivalents as presented in the statement of assets and liabilities and the statement of cash flows include bank checking accounts and short term securities with an original maturity of less than 90 days.

Investments and Related Investment Revenue and Expense

All related revenue and expenses attributable to these transactions are reflected on the statement of operations commencing on the settlement date unless otherwise specified by the transaction documents.

The Company accrues interest income if it expects that ultimately it will be able to collect it. Generally, when an interest payment default occurs on a loan in the portfolio, or if management otherwise believes that the issuer of the loan will not be able to service the loan and other obligations, the Company will place the loan on non-accrual status and will cease recognizing interest income on that loan until all principal and interest is current through payment or until a restructuring occurs, such that the interest income is deemed collectible.

However, the Company remains contractually entitled to this interest. The Company may make exceptions to this policy if the loan has sufficient collateral value and is in the process of collection and the amount of collectible interest can be reasonably estimated.

For loans with contractual PIK (payment-in-kind) interest income, which represents contractual interest accrued and added to the loan balance that generally becomes due at maturity, we will not accrue PIK interest if we believe that the PIK interest is no longer collectible, including if the portfolio company valuation indicates that such PIK interest is not collectible. Loan origination fees - net of direct loan origination costs, original issue discounts that initially represent the value of detachable equity warrants obtained in conjunction with the acquisition of debt securities and market discounts or premiums are accreted or amortized using the effective interest method as interest income over the contractual life of the loan. Upon the prepayment of a loan or debt security, any unamortized net loan origination fee will be recorded as interest income. Loan exit fees that are contractually required to be paid at the termination or maturity of the loan will be accreted to interest income over the contractual term of the loan. We suspend the accretion of interest income for any loans or debt securities placed on non-accrual status. We may also collect other prepayment premiums on loans. These prepayment premiums are recorded as interest income as earned. Dividend income, if any, will be recognized on the ex-dividend date.

Certain expenses related to legal and tax consultation, due diligence, rating fees, valuation expenses and independent collateral appraisals may arise when the Company makes certain investments. To the extent that such costs are not classified as direct loan origination costs, these expenses are recognized in the statement of operations as they are incurred.

Net Realized Gains or Losses and Net Change in Unrealized Appreciation or Depreciation

Realized gains and losses in investments are calculated using the specific identification method. We measure realized gains or losses as the difference between the net proceeds from the repayment or sale and the amortized cost basis of the investment, without regard to unrealized appreciation or depreciation previously recognized, but considering unamortized upfront fees and exit fees. Net change in unrealized appreciation or depreciation reflects the change in portfolio investment values during the reporting period, including any reversal of previously recorded unrealized appreciation or depreciation, when gains or losses are realized.

Classification of Investments

We classify our investments by level of control. As defined in the 1940 Act, control investments are those where there is the ability or power to exercise a controlling influence over the management or policies of a company. Control is generally deemed to exist when a company or individual possesses or has the right to acquire within 60 days or less, a beneficial ownership of 25% or more of the voting securities of an investee company. Affiliated investments and affiliated companies are defined by a lesser degree of influence and are deemed to exist through the possession outright or via the right to acquire within 60 days or less, beneficial ownership of 5% or more, but less than 25%, of the outstanding voting securities of another person. Twelve of the Company's investments are classified as non-control/non-affiliated investments as of March 31, 2013 and December 31, 2012, respectively. One of the Company's investments is classified as affiliated as of March 31, 2013 and December 31, 2012, respectively.

Valuation of Investments

Valuation analyses of the Company's investments are performed on a quarterly basis pursuant to ASC 820, *Fair Value* Measurements. ASC 820 defines fair value, establishes a framework for measuring fair value in accordance with applicable accounting guidance and expands disclosure of fair value measurements.

Pursuant to ASC 820, the valuation standard used to measure the value of each investment is fair value defined as, “the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.” Investments are recorded at their fair value at each quarter end (the measurement date).

Fair Value Investment Hierarchy

Accounting standards establish a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

Level 1	Quoted prices (unadjusted) for identical assets or liabilities in active public markets that the entity has the ability to access as of the measurement date.
Level 2	Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.
Level 3	Significant unobservable inputs that reflect a reporting entity’s own assumptions about what market participants would use in pricing an asset or liability.

Valuation Process

Investments are measured at fair value as determined in good faith by our board of directors, based on, among other factors, consistently applied valuation procedures on each measurement date.

The Company engages an independent external valuation firm to review all Level 3 investments, at least annually. This external review is used as a key input in connection with the determination of the fair value of the Company's investments.

The board of directors undertakes a multi-step valuation process at each measurement date.

* Our valuation process begins with each investment valued by the investment professionals of our investment adviser responsible for the investment.

* Preliminary valuation conclusions are documented and discussed with our management and our investment adviser.

* The audit committee of our board of directors reviews and discusses the preliminary valuations.

* At least once annually, the valuation for each portfolio investment is reviewed by the independent valuation firm.

* The board of directors discusses valuations and determines the fair value of each investment in our portfolio in good faith, based upon the input of our management, our investment adviser, the independent valuation firm and the audit committee.

Valuation Methodology

The following section describes the valuation methods and techniques used to measure the fair value of the investments.

Fair value for each investment will be derived using a combination of valuation methodologies that, in the judgment of our management are most relevant to such investment, including, without limitation, being based on one or more of the following: (i) market prices obtained from market makers for which our management has deemed there to be enough breadth (number of quotes) and depth to be indicative of fair value, (ii) the price paid or realized in a completed transaction or binding offer received in an arms-length transaction, (iii) market approach (enterprise value), (iv) income approach (discounted cash flow analysis) or the (v) bond yield approach.

The valuation methods selected for a particular investment are based on the circumstances and on the level of sufficient data available to measure fair value. If more than one valuation method is used to measure fair value, the results are evaluated and weighted, as appropriate, considering the reasonableness of the range indicated by those results. A fair value measurement is the point within that range that is most representative of fair value in the circumstances.

The determination of fair value using the selected methodologies takes into consideration a range of factors including, but not limited to, the price at which the investment was acquired, the nature of the investment, local market conditions, trading values on public and private exchanges for comparable securities, current and projected operating performance and financing transactions subsequent to the acquisition of the investment, compliance with agreed upon terms and covenants, and assessment of credit ratings of an underlying borrower.

In most cases we use the bond yield approach for valuing our level 3 debt investments, as long as we deem this method appropriate. This approach entails analyzing the interest rate spreads for recently completed financing transactions which are similar in nature to ours by companies that are similar to us, in order to assess what the range of effective market interest rates would be for our investment if it were being made on or near the valuation date. Then all of the remaining expected cash flows of the investment are discounted using this range of interest rates to determine a range of fair values for the debt investment.

The fair value of equity securities, including warrants, in portfolio companies often times considers the market approach which applies market valuation multiples of publicly-traded firms or recently acquired private firms engaged in businesses similar to those of the portfolio companies. This approach to determining the fair value of a portfolio company's equity security will typically involve: (1) applying to the portfolio company's trailing twelve month EBITDA (earnings before interest, taxes, depreciation and amortization) a range of enterprise value to EBITDA multiples that are derived from an analysis of comparable companies, in order to arrive at a range of enterprise values for the portfolio company; then (2) subtracting from the range of enterprise values balances of any debt or equity securities that rank senior to our equity securities; and (3) multiplying the range of equity values by the Company's ownership share of such equity to determine a range of fair values for the Company's equity investment.

We also use the income approach which discounts a portfolio company's expected future cash flows to determine its net present enterprise value. The discount rate used is based upon the company's weighted average cost of capital, which is determined by blending the cost of the company's various debt instruments and its estimated cost of equity capital. The cost of equity capital is estimated based upon our market knowledge and discussions with private equity sponsors.

These valuation methodologies involve a significant degree of judgment. As it relates to investments which do not have an active public market, there is no single standard for determining the estimated fair value. Valuations of privately held investments are inherently uncertain, and they may fluctuate over short periods of time and may be based on estimates. The determination of fair value may differ materially from the values that would have been used if a ready market for these investments existed. In some cases, fair value of such investments is best expressed as a range of values derived utilizing different methodologies from which a single estimate may then be determined.

Consequently, fair value for each investment may be derived using a combination of valuation methodologies that, in the judgment of our management, are most relevant to such investment. The selected valuation methodologies for a particular investment are consistently applied on each measurement date. However, a change in a valuation methodology or its application from one measurement date to another is possible if the change results in a measurement that is equally or more representative of fair value in the circumstances.

Capital Gains Incentive Fee

Under GAAP, the Company calculates the capital gains incentive fee as if the Company had realized all investments at their fair values as of the reporting date. Accordingly, the Company accrues a provisional capital gains incentive fee taking into account any unrealized gains or losses. As the provisional incentive fee is subject to the performance of investments until there is a realization event, the amount of provisional capital gains incentive fee accrued at a reporting date may vary from capital gains incentive fee that is ultimately realized and the differences could be material.

Deferred Financing Costs

Deferred financing costs are made up of deferred debt issuance costs and deferred equity offering costs. The deferred debt issuance costs consist of fees and other direct costs incurred by the Company in obtaining debt financing from its lender and are recognized as assets and are amortized as interest expense over the term of the credit facility. The deferred equity offering costs consist of legal fees and other costs incurred by the Company in conjunction with raising external capital and are recognized as an asset and recorded as a reduction to contributed capital when the Company raises equity. The balance of deferred financing costs as of March 31, 2013 and December 31, 2012 was

$171,135, of which $122,468 relates to deferred debt issuance costs and $48,667 relates to deferred equity offering costs, and $180,786, of which $132,119 relates to deferred debt issuance costs and $48,667 relates to deferred equity offering costs, respectively. The amortization expense relating to deferred debt issuance costs during the three months ended March 31, 2013 and the three months ended March 31, 2012 was $9,651 and $8,853, respectively.
The amortization expense relating to the deferred equity offering costs during the three months ended March 31, 2013 and the three months ended March 31, 2012 was $0 and $15,509, respectively.

Dividends and Distributions

Dividends and distributions to common stockholders are recorded on the ex-dividend date. The amount to be paid out as a dividend or distribution is determined by the Board and is generally based upon the taxable earnings estimated by management. Net realized capital gains, if any, are distributed at least annually, although the Company may decide to retain such capital gains for investment. The Company adopted a dividend reinvestment plan that provides for reinvestment of our dividends and other distributions on behalf of our stockholders, unless a stockholder elects to receive cash. As a result, if the Board authorizes, and we declare, a cash dividend or other distribution, then our stockholders who have not “opted out” of our dividend reinvestment plan will have their cash distribution automatically reinvested in additional shares of our common stock, rather than receiving the cash distribution. No action is required on the part of a registered stockholder to have their cash dividend or other distribution reinvested in shares of our common stock.

Income Taxes

HCC LLC was treated as a partnership for federal and state income tax purposes and did not incur income taxes. Accordingly, no provision for income taxes has been made in the accompanying financial statements, as each member of HCC LLC was individually responsible for reporting income or loss, to the extent required by federal income tax laws and regulations, based upon its respective share of HCC LLC's revenues and expenses as reported for income tax purposes. The Company intends to elect to be treated, and intends to qualify annually thereafter, as a RIC under Subchapter M of the Code. To obtain RIC tax benefits, the Company must distribute at least 90% of ordinary income and realized net short-term capital gains in excess of realized net long-term capital losses, if any, out of the assets legally available for distribution. In order to avoid certain excise taxes imposed on RICs, the Company currently intends to distribute during each calendar year an amount at least equal to the sum of (1) 98% of ordinary income for the calendar year, (2) 98.2% of capital gains in excess of capital losses and (3) any ordinary income and net capital gains for preceding years that were not distributed during such years and on which the Company paid no U.S. federal income tax.

HCC LLC's and the Company’s tax returns are subject to examination by federal, state and local taxing authorities. Because many types of transactions are susceptible to varying interpretations under federal and state income tax laws and regulations, the amounts reported in the accompanying financial statements may be subject to change at a later date by the respective taxing authorities. The Company recognizes the financial statement benefit of a tax position following an audit. For tax positions meeting the more-likely-than-not threshold, the amount recognized in the financial statements is the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement with the relevant tax authority. Penalties or interest that may be assessed related to any income taxes would be classified as other operating expenses in the financial statements. Based on an analysis of our tax position, there are no uncertain tax positions that met the recognition or measurement criteria. The Company has no amounts accrued for interest or penalties as of March 31, 2013. Neither HCC LLC nor the Company is currently undergoing any tax examinations. The Company does not anticipate any significant increase or decrease in unrecognized tax benefits for the next twelve months. The 2011 and 2012 federal tax years for HCC LLC and the Company remains subject to examination by the IRS. The 2011 and 2012 state tax years for HCC LLC remain subject to examination by the California Franchise Tax Board.

Recent Accounting Pronouncements

From time to time, new accounting pronouncements are issued by the FASB or other standards setting bodies that are adopted by the Company as of the specified effective date. The Company believes that the impact of recently issued standards that are not yet effective will not have a material impact on our financial statements upon adoption.

Note 3. Borrowings

HCC LLC entered into a 6 year, $30.0 million credit facility on August 24, 2011 with JMP Group LLC. The credit facility has a two year revolving period with maximum outstanding amounts that began at $20 million and increased at a rate of $2.5 million per quarter thereafter until maximum outstanding available reached $30.0 million in July 2012. The maximum amount outstanding is also limited by a covenant which restricts borrowings to be less than 2.0 times the Net Tangible Asset Value of HCC LLC. At the end of the two year revolving period the outstanding balance will amortize evenly at 5% in each of the following 16 consecutive quarters with the final 20% due at maturity in August 2017. The credit facility carried an interest rate of LIBOR + 7.00%, with a LIBOR floor of 1.50%, or the Prime rate + 4.75%. The credit facility also had an unused line fee of 0.50% per year. The Company paid an origination fee of 0.50% or $150.0 thousand at closing. The outstanding balance on the facility was $22.2 million and $28.2 million as of March 31, 2013 and December 31, 2012, respectively.

On March 25, 2013, HCC LLC and HCAP entered into an amendment to the credit facility with JMP Group LLC, whereby, upon completing our IPO (which closed on May 7, 2013) and satisfaction of certain other closing conditions, we have secured a revolving credit facility with JMP Group LLC on the same or substantially similar terms as the initial credit facility entered into between JMP Group LLC and HCC LLC. Each loan origination under this credit facility is subject to the satisfaction of certain conditions. This secured revolving credit facility will provide, subject to certain conditions and limitations, up to an aggregate of $50.0 million of revolving borrowings until April 1, 2014, but that amount may be reduced by us unilaterally upon giving notice to JMP Group LLC. After April 1, 2014, the amount outstanding thereunder will become a term loan payable in fourteen consecutive quarterly installments (beginning on April 1, 2014), each in an amount equal to 5% of the term amount, and with the final payment of any other outstanding amounts due on the maturity date of August 24, 2017. Borrowings under the secured revolving credit facility will bear interest at an annual rate equal to either (i) LIBOR + 4.50% or (ii) the Prime Rate + 2.25%, at our election and subject to increases during a default under the credit facility.

Debt Maturities

The contractual obligations under the revolving credit facility as of March 31, 2013 and December 31, 2012 were as follows:

As of March 31, 2013	As of December 31, 2012